

Asia Financial Institutions

Retail banking in Asia

Actionable insights
for new opportunities

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Foreword

Retail banking in Asia is on the cusp of a new era—an era of amazing growth and opportunities but also an era that will see downward pressure on returns. Asia will reach over USD 900 billion in retail banking revenue by 2020, growing at about 14 percent per year from 2010. It is expected to be the second largest wealth management region globally after the United States, with more personal financial assets residing here in Asia than Europe by 2015. This is also a market where we are seeing and will continue to see rapid shifts in three consumer behaviours—heightening demands on frontline services, fast adoption of new mobile platforms, and increasing need for credit and a larger variety of products alongside growth of the middle class and urbanization, amongst others.

But these opportunities are not easy to capture.. Rapidly shifting consumer behaviour calls for a potential complete revamp of the traditional operating models—roles of the branches may change, new channels will need to be introduced, and new capabilities will need to be built. Non-traditional competition will enter the market, vying with banks for the same revenue pools. New regulatory requirements as well as growing risks with new segments will continue to add to the cost of retail banking.

In the following articles, we hope to offer insights that will be actionable in this new era. They are the work of practitioners from McKinsey's Asia Retail Banking Practice and are based on our proprietary data and experience from working with clients across Asia.

We hope that they will help stimulate new thinking that will be useful for retail banking executives interested in this market.



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March 2013



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Contents



Chapter 1

Innovation in Asian retail banking business models 1



Chapter 2

Digital banking in Asia 9



Chapter 3

Is the branch obsolete in a multichannel world? 23



Chapter 4

Creating the customer-centric retail bank 35



Chapter 5

Next-generation productivity improvement:
Sales transformation 2.0 47



Chapter 6

Four innovative ways to create actionable insights
from customer data 59



Chapter 7

Getting into the revenue flow: Insights from
McKinsey's Asia-Pacific Payment Map 67



Chapter 8

The rise of Asia's private banking markets 75



About us

McKinsey's Retail Banking Practice in Asia 91



Chapter 1

Innovation in Asian retail banking business models

Kenny Lam, Joydeep Sengupta, and Renny Thomas

Key highlights:

- Despite high revenue growth driven by emerging Asian economies, Asian retail banks are experiencing downward pressures on returns.
- New regulatory requirements, higher risk due to a slowing global economy, and increasing customer sophistication mean that banks must innovate to grow.
- Asian banks of the future will be universal and multitalented, growing through an innovative multichannel infrastructure, next-generation risk skills, and privileged customer insights.
- On customer insights, it is not just about the power of analytics and the wealth of data but also turning a bank's analytics into something tangible, actionable, and "bite-size" for the frontline to execute.

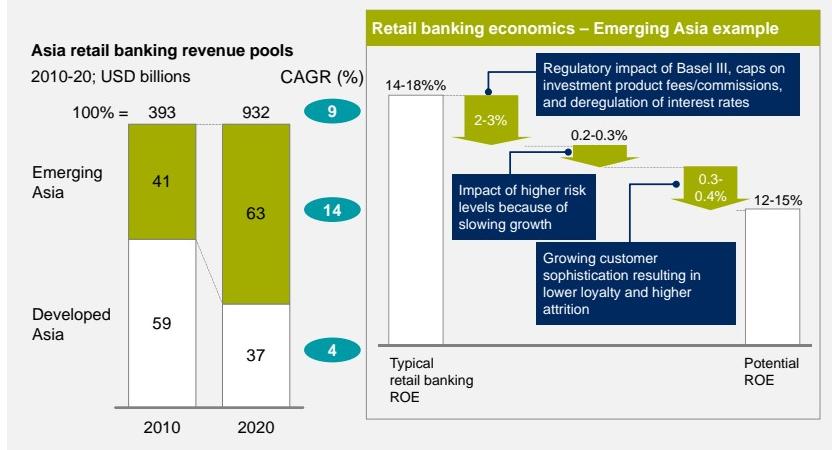
Asian retail-banking revenue continues to climb as global growth shifts eastward. In the present decade, 2010 to 2020, Asian banking revenue pools are expected to rise to \$932 billion, more than doubling in size and growing at an overall annual rate of 9 percent. Furthermore, emerging Asian countries are accounting for most of the high growth, and will soon have attracted more revenue in absolute terms than developed Asia.

Despite the high revenue growth, however, Asian retail banking is also experiencing downward pressure on returns. While typical retail banking ROE can be 14 to 18 percent, these rates are being driven down by the regulatory impact of Basel III, the impact of higher risk levels because of slowing growth, and rising customer sophistication, which is resulting in lower loyalty and higher attrition (Exhibit 1).

Exhibit 1

Despite high revenue growth driven by emerging Asia, there are downward pressures on returns.

ILLUSTRATIVE



To deliver continued growth and create further value, Asian universal banks will need to be multitalented innovators in one or more of three dimensions of retail banking:

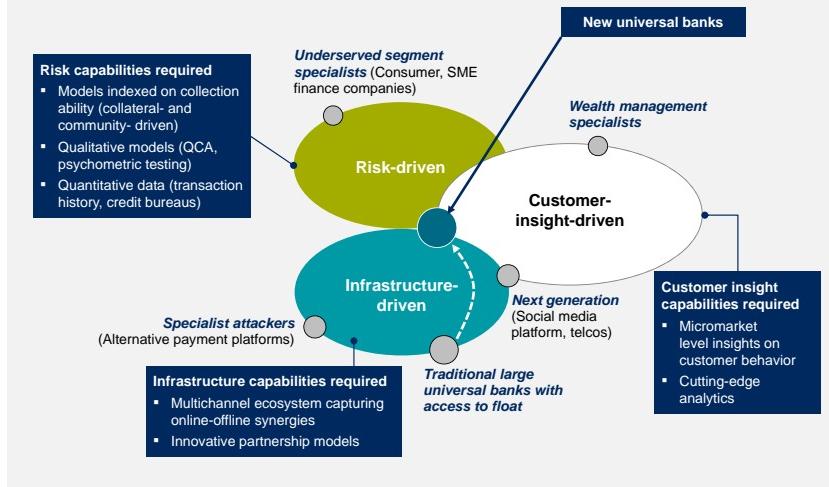
- **Distribution.** An innovative distribution infrastructure will address new challenges. While access to a physical network continues to drive share of primary banking relationships, banks need to prepare for a more multichannel environment to respond to customers and manage economics.
- **Credit-risk management.** Next-generation risk skills will profitably target underserved segments such as SMEs and mass market. Banks will need to build underwriting models that fully leverage qualitative and quantitative information and the available collateral in these segments.
- **Customer insights.** Banks can create privileged customer insights from existing data. A more granular approach to growth can be taken by developing deeper insights along multiple dimensions, including geography (for example, micromarkets) and customer behavior (such as digital usage).

In planning their innovation strategies, banks will need to assess their own position and capabilities and the competitive terrains on which they operate. For

some retail banks, the need for innovation may exceed the limits of what they consider practical, but those capabilities will have to be acquired for the bank to continue to compete and grow. In which of these dimensions is innovation practical for the bank? What forms of innovation will bring the bank advantages? Wherein lie the greatest threats from potential attackers, and how significant could the damage be? What are the implications of innovation for organization structures and talent in the retail-banking context? These and related questions can help orient retail banks for the innovation journey that lies before them. Exhibit 2 presents a sketch of the new universal bank, with fully developed innovative capabilities, lying at the intersection of the three dimensions of innovation: distribution infrastructure, customer insights, and new risk models.

Exhibit 2

The 3 dimensions for potential innovation to beat the downward pressure on returns.



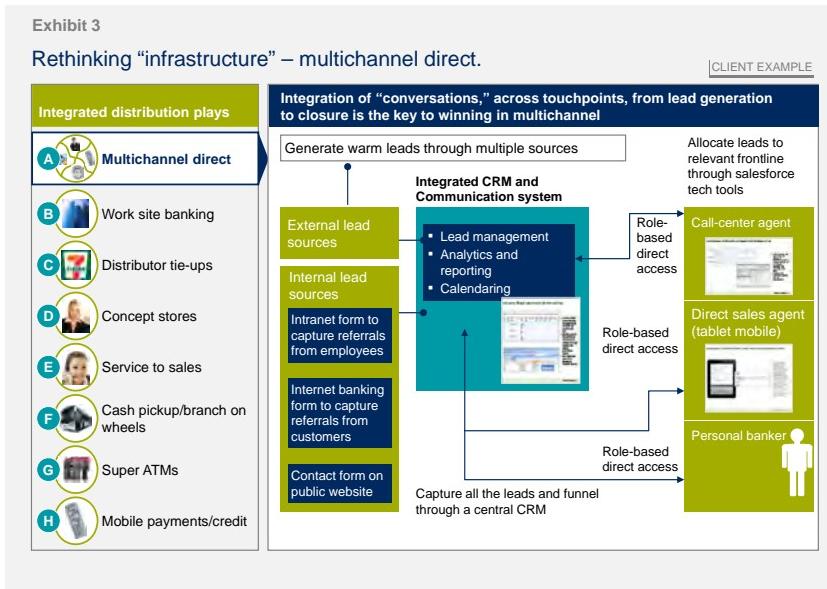
An innovative distribution infrastructure

Over 80 percent of banking consumers in Asia are already using multiple channels, with an average of six touch points per customer in play. The proliferation of distribution channels has, however, entailed greater complexity and a lack of coordination that have often led to poor customer experience. It is not surprising, therefore, that McKinsey analysis has revealed that around 60 percent of Asian banking consumers believe that “shopping around” for financial products is worth the effort.

Infrastructure innovation can be expensive. For retail banks in emerging Asia, distribution architecture, including branches, automatic-teller machines, call centers, and IT, can account for 50 to 70 percent of non-people costs. These investments, furthermore, have a longer breakeven timeline in new markets. Nevertheless, when successfully executed, a multichannel approach brings significant benefits. Conversion rates improve in all steps of the funnel as banks present a much more hospitable and fluidly interactive suite of consumer-facing touch points. Since frontline and back-office collaboration is enabled across channels and value-chain steps, targeted cross-selling and follow-up processes are systematically embedded into the bank's customer-portfolio management.

One obvious aspect of the successful multichannel approach is a tightly linked online-offline interface. While most consumers are slow to purchase financial products online, McKinsey research performed in collaboration with Google has demonstrated dramatically that consumer purchasing-decision journeys are highly influenced by online research. In retail banking, as in other retail sectors, "research online, buy offline" is the watchword that characterizes more and more consumer behavior.

In addressing the innovation demands of their environments, retail banks are rethinking their approach to infrastructure. New avenues that have been opened include work-site banking, retail-store tie-ins, and mobile payments and credit. Exhibit 3 explores the possibilities in rethinking another avenue: multichannel direct. Here the consumer conversation is integrated across touch points, from lead generation to closure. The integrated CRM approach unites and aligns all consumer-facing infrastructure: call-center agents, direct-sales agents, personal bankers, and all electronic channels.



Next-generation risk skills

In retail banks with superior risk and capital management, underwriting and collections models are key drivers of value. Innovation in underwriting can be pursued through distinctive qualitative models, built on objectivity and the methodical collection of qualitative information. Additionally, *quantitative data* can be deployed with greater distinctiveness, including internal data (such as past history and transaction data) and external data (including credit bureau, social, and retail data).

Qualitative credit underwriting

In the qualitative approach (called qualitative credit assessment, or QCA), qualitative factors, which are normally considered judgment calls, are assessed in a highly objective and consistent way. For the predictive model, the ingoing qualitative information is gathered and applied in a statistical approach. Redundancy is deliberately introduced into the model to add robustness to judgment, and business considerations are afforded a heavy weight. QCA is well suited to harness human expertise in model development; it captures hindsight with back-testing and promotes the exercise of informed judgment in underwriting. The QCA model-building process yields a user-friendly assessment tool, with 20 or 25 questions that can be completed in less

than one hour. Fewer than 10 percent of applicants require further analysis, with specific issues treated in a separate form.

Unconventional insights from unconventional data

In credit-risk assessments, several sources can be mined for unconventional insights. Retail banks usually have an effective credit-risk model for evaluating applicants who have a credit history. For these potential customers, traditional underwriting data, such as demographics, may not be sufficient for assessing risk. However, when those data are augmented by data from a nontraditional source, such as retail purchasing data—including location of purchases and consistency of shopping pattern—the predictive power of the credit-risk assessments is enhanced, sometimes considerably.

Privileged customer insights

The large data pools to which banks have access, including the enormous data sets on their own customer base, provide the foundation for the third dimension of innovation.

Better management of existing customer relationships

To identify and intensify relationships with their own high-value customers, banks have the data they need at their fingertips. Pertinent customer data sets can enable a deeper and more granular analysis of the customer base, establishing customers' value to the bank by customer type and segment. Banks can then accordingly design and align channels and tailor and price services and products to foster more profound relationships with high-potential customers, while better managing costs in lower-value segments.¹

Future growth in targeted segments and micromarkets

Banks can create privileged consumer insights about targeted segments and geographies from generally available demographics and other data. McKinsey Digital Consumer Research, for example, has identified a segment of “digital high value” consumers in India that is already 27 million strong and is expected to grow to 70 million by 2015. These consumers hold 31 percent of household savings, amounting to \$45 billion today and estimated to reach almost \$150 billion by 2015. To address these Internet-using professionals going forward, retail banks will need a highly interactive online channel, closely integrated across the distribution infrastructure.

¹ For a closer look at how retail banks can leverage customer data, see Chapter 6, “Four innovative ways to create actionable insights from customer data.”

In one sense the term “micromarket” is a misnomer in Asia, since granular growth opportunities in particular geographies can each involve millions or tens of millions of consumers. Data can allow banks to analyze the consumer and competitor landscapes down to a city view or even a neighborhood view. The object is to identify the areas in which the bank’s highest-potential targeted segments are concentrated, so that they may be addressed with the appropriate resources. Of particular importance for retail banking in emerging Asia are scores of attractive “middleweight” cities, where mass-affluent and affluent consumer segments are growing fast. Each of these cities can have millions of consumers in these high-value segments and yet they may be underserved.



The dynamic by which retail banks in Asia are simultaneously experiencing high revenue growth and a downward pressure on returns is very real and promises to continue for the foreseeable future. Opportunities for growth, both intensive (within the customer base) and extensive (outside the base) are present and even proliferating across Asia and especially emerging Asia. In these opportunities lies the answer to the problem of diminishing returns; however, all opportunities are not created equal for all banks. Resources are limited and existing capabilities and the competitive landscape must be carefully evaluated before any opportunity can be profitably pursued.

Yet the limitations present for any one retail bank do not exempt that bank from the innovations that will characterize the universal bank of the coming decade. These innovations are already emerging in the three dimensions we have been discussing: a smart, multiple-channel integrated distribution infrastructure; new and unconventional approaches to assessing risk in underserved segments; and the deployment of customer and demographic data to achieve granular profiles of promising new segments and geographies as well as the existing customer base.

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Chapter 2

Digital banking in Asia

Joe Chen

Key highlights of this article:

- Rapid technological development and new digital consumer behaviors are combining into a storm that is sweeping retail banking across Asia
- Even in developing Asian markets, new digital consumers value experience, convenience, control, and value-added services more than low pricing
- Potential bank strategies range from “multichannel integrators” supplementing branches to “digital leaders” targeting savvy consumers to “market shapers” expanding beyond financial services
- As in start-ups, successful implementation will depend on a fast test-and-learn approach that challenges traditional retail banks’ talent models and organizational cultures

Banks in Asia have a unique chance to build on digital innovation and transform what a bank is. But they must move quickly to capitalize on the enormous potential bottom-line impact.

Around the world, conditions for banking’s “digitalization” are now optimal. Faster, easier connectivity and powerful, user-friendly smart devices are reinforcing profound behavioral changes among consumers, who now reassess and remake their choices almost continuously. At the same time, cloud computing, mobility, big data, and related enterprise-technology innovations are generating unprecedented revenue and cost reduction opportunities. The result is a once-in-a-generation chance to create a new customer-centric, digital business model for banking.

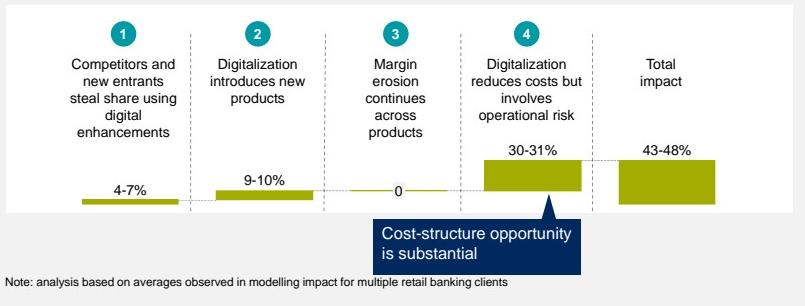
Getting it right will be essential for banks to survive a battle that is already under way. Attackers ranging from start-ups like Square to longtime giants Google and PayPal have encroached on traditional banking territory, with digital payment as the main point of entry. An analysis of the potential impact of digital on several retail banks showed that almost half of profits are at

stake (Exhibit 1). To date, several of the fastest movers have been in developed markets, where new regulatory constraints, higher risk capital needs, and historically low interest rates have compressed banks' margins. But even Asian banks that have been insulated from some of these pressures are seeing their own form of digital upheaval, reflecting the sheer scale of technology change on the world's most populous continent—where tens of millions of young, middle-class and affluent consumers are becoming digital-centric.

Exhibit 1

About 45 percent of net profit is at stake.

Impact from digital, % of net profit



Indeed, despite the very different contexts, customer expectations in Asian and Western markets are converging on many important points. This is especially visible among the technology-savvy, self-directed customers that are the earliest adopters—and that account for much of both the affluent category and Generation Y. These consumers want not just 24-hour access but the ability to use and manage their money by whatever channel they want, wherever they happen to be. They want greater control over about their financial services, with a single, consistent, and engaging experience from the branch to their mobile devices. And they want fair, transparent pricing—not necessarily the cheapest.

This is a far more complex set of needs than in the days when digital was primarily a price-driven, direct-bank proposition, with stripped-down products and services in exchange for higher deposit rates or cheaper loans. Now, digital must be integral to a new type of banking.

Just how new (and how digital) is a matter of strategic choice. A bank can be a “multichannel integrator” that incorporates digital offerings into a branch-based foundation, a “digital leader” that opts for a truly digital-centric model, or a “shaper” that builds a disruptive “Bank 2.0” from the ground up. A few

sophisticated banks are pursuing multiple strategies concurrently, targeting different digital consumer segments.

In fact, the three major paths involve the same fundamental changes, differing mainly in degree. All banks will need to think beyond just pricing and the Internet, offering consumers compelling value-added services, superior multichannel experience (across online, mobile, and offline), and compelling value-added services, all while revamping their processes and building new capabilities. And they will have to move fast, following a new test-and-learn approach that encourages innovation, adapts quickly, and keeps trying new ideas.

Meet your new digital customer

One of the surprises confronting banks in Asia is how quickly local consumers have adopted digital technologies. By the end of 2011, China and India already ranked first and third in the global league table for number of Internet users. Mobile platforms have been critical: in China, 65 percent of mobile-phone users regularly access the Internet via their phones, while in India, mobile-only Web browsers are expected to comprise 55 percent of the total Internet user base by 2015.

Surfing the Web...and mobile

With the rise of mobile comes the rise of mobile banking. In 2011, for the first time in its 13-year history, the McKinsey Personal Financial Services survey² found that Asian consumers were visiting branches less often than in earlier years. And the percentage drop recorded in Asia's emerging markets—26 points—was almost the same as the 29-point fall seen in the region's developed markets. In mirror image, digital-channel usage increased by 36 percent in developed markets (where people now use digital channels more than branch and telephone banking put together), and 39 percent in emerging Asia, although on a much smaller base (Exhibit 2).

Even in markets where financial-services consumers are still purchasing most products in person, the Internet is playing an increasingly crucial role in the decision-making process. A 2012 McKinsey survey of Indian Internet users found that, for example, about 70 percent of users who had acquired credit cards in the preceding year used the Internet for product research, as did 66 percent of users who bought health insurance and 53 percent who took out personal loans.

² "Customer first: New expectations for Asia's retail banks," Tracy Cowap, Kenny Lam, and Jatin Pant, February 2012 (mckinsey.com).

Exhibit 2

Customers are leaving branches for Internet and mobile banking.

Monthly usage frequency



- Two “firsts”**
- First ever drop in branch usage since 1998
- First ever data showing that Developed Asia consumers use new channels (Internet/mobile) more than traditional channels (telephone and branch)

Multichannel hoppers

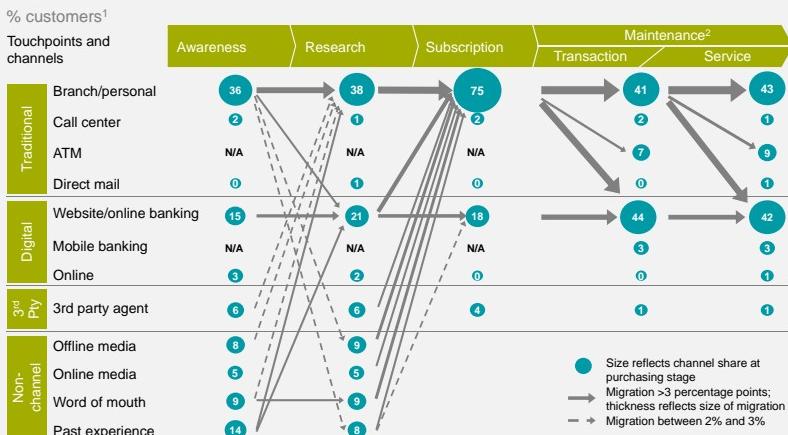
When buying financial-services products, consumers across Asia are following much more complex routes (Exhibit 3) than the old “purchasing funnel” would imply. Between the “awareness” and “maintenance” stages, 83 percent of buyers move across multiple channels—using as many as 5 channels for researching new products, and about 1.8 channels for servicing their existing products.

With so many pathways available, ensuring that consumers reach the hoped-for destination—a purchased product or service—requires more attention and effort.

Exhibit 3

Today's consumers are multi-channel hoppers.

KOREA



1 Only most important paths are shown here

2 All arrows to maintenance activities are directly from Subscription phase (i.e., transaction and service phases are not sequential)

SOURCE: 2007 and 2011 McKinsey Personal Financial Services surveys; McKinsey analysis

Beyond pricing

Asian digital consumers' eagerness to move across channels points to a deeper finding: when it comes to digital banking, consumer needs in Asia are increasingly similar. Two very different markets, Hong Kong and India, illustrate a convergence in which convenience and control matter far more than pricing.

When asked about what they like about using their mobile devices, Hong Kong respondents to the 2012 McKinsey mobile-payments survey cited familiar factors such as speed and convenience—being able to use multiple payment sources with one device, for instance, or not having to carry credit cards. In addition, over 40 percent liked the access to deals that mobile devices gave them, and the greater control they could exercise over their finances.

India's digital-banking customers showed similar preferences, citing good customer experience, flexibility, and customization as the main features they wanted from digital banking. Pricing came in a distant fourth place, even among lower-income consumers. For wealthier, more urban "digital high value" customers, pricing barely even registered as a concern (Exhibit 4).

Exhibit 4

'Digital high value' consumers value experience, flexibility and customization over pricing.

Consumer preferences

Score on a scale of 10



¹ Customers in 20–45 age group; Market Research Society of India socioeconomic classification categories A & B, Tier 1 and Tier 2, household income of INR 600,000 (~\$11,000) and above, heavy users of Internet.

SOURCE: 2011 McKinsey Personal Financial Services surveys; McKinsey analysis

Three options for the future

Meeting these new customer expectations will not be easy for most Asian banks, whose operations and service models have long depended even more heavily on sprawling in-person branch networks than their peers in other regions. (For more detail on the evolution of the branch, see Chapter 3, "Is the branch obsolete in a multichannel world?") Yet examples from Europe and North America nevertheless point to three broad options that together form a spectrum of strategic ambition.

Multichannel integrator: Optimize for profitability

The most attainable of the three strategies, especially for branch-heavy incumbents, weds a sophisticated, client-centric digital model to an existing branch-based offering. Branches would remain an important channel for sales of complex products, while direct channels would become the primary medium for fulfillment, service inquiries, and sales of simple products. The transition would allow the bank to gradually optimize its high-street real-estate footprint, even as it increases penetration and cross-sales among tech-oriented consumer segments.

Several leading European and North American institutions are already implementing this model successfully. One of the largest European banks is completely revamping its sales process to facilitate online applications, with branches serving in a supplemental role when express electronic fulfillment is not possible. A North American bank has applied the same idea with a specialty focus, using a branch-plus-digital format to offer integrated personal and business cash-management and investment services to the time-constrained (and expensive-to-serve) small-business owners who traditionally rely heavily on branch services.

Digital leader: Service for the digital consumer

The middle range of the spectrum pushes the logic further by facilitating a digital-centric banking concept, and therefore relies even more heavily on direct channels for sales of all types of products and services. The target customers are typically younger and more tech aware, but the operating model is ultra-lean, especially when it comes to branches. Only a few thoughtfully designed, high-visibility “showcase” locations remain, more for new-customer acquisition, brand reinforcement, and solving customer problems than for day-to-day sales and transactions.

Incumbent institutions that have adopted this strategy typically create separate brands, with Portugal’s Activobank owned by Millennium and Italy’s CheBanca! by Mediobanca. CheBanca!, launched in 2008, has a network of just 44 branches, but as of mid-2012 it was managing half a million customers with €11.6 billion in deposits—for an average of more than €20,000 per customer.

Market shaper: Building ‘bank 2.0’

The final, most challenging, and most potentially disruptive strategy is to build a pioneering multicategory value proposition, with financial services as just one of many components. Although more typically the offering of nonfinancial attackers, such as Asian e-commerce giants Rakuten of Japan and Alibaba of China, a few new platforms have been launched by institutions willing to completely reassess not only how they serve their customers but also what services they provide.

Spain's La Caixa provides an example through its market-leading mobile platform, CaixaMóvil. Rather than offer just the typical mobile-banking app, CaixaMóvil is more like an app store, with a growing suite of more than 50 financial and nonfinancial applications covering everything from payments and financial management to shopping and entertainment. A few seem designed just to make customers happy, such as the "Stock Music" app, which indicates how stocks are performing by varying the volume of the user's music—obviating the need to watch a screen. And by housing the apps separately, La Caixa puts its customers in control over whether—and to what degree—they interact with nonfinancial services.

So far the mobile platform has attracted over 2.6 million users, with growth of at least 13 percent annually and, as of February 2012, a market-leading 30 percent share of the highly competitive Spanish online banking business.

Getting the digital bank right

The emergence of digital banking therefore offers banks much more than just productivity gains in core banking processes. Instead, the disruption of existing business models is leading to a much broader transformation in how banks acquire, develop, and retain customers (see Chapter 3, "Is the branch obsolete in a multichannel world?") Transforming into a successful digital bank will thus require four broad types of changes: in offerings, channels, processes, and capabilities (in areas such as IT and marketing). The level of change will naturally vary depending on the bank's starting point and ambition, but most will need to reexamine all four to at least some degree (Exhibit 5).

Exhibit 5

Transition on each level is profound.

	Element	FromTo
Offering	<ul style="list-style-type: none"> ▪ No. of products (e.g., savings) ▪ Revenues from digital-only products 	45 0%	4 5-10%
Channel	<ul style="list-style-type: none"> ▪ % remote advice ▪ Avg. distance to branch ▪ FTEs/branch 	0% 5 min 6-8 FTEs	50% 15 min 2-4 FTEs
Process ²	<ul style="list-style-type: none"> ▪ Transactions/services ▪ Sales ▪ Advice 	75% 10-20% 10%	100% 100% 100%
Capabilities	<ul style="list-style-type: none"> ▪ IT ▪ Data processing ▪ Marketing ▪ Partnerships 	Transactions, risk management Retrospective Traditional Few	Straight-through processing; customization Real-time Digital/social Many

¹ Full-time equivalent.

² % digitalized.

From low prices to high style

For initial traction in competitive markets, most digital offerings now include one or two low-price “hook” products. Yet that concession to price competition should not obscure the larger reality: today’s digital customers focus less on pricing and more on the total customer experience. That is good news for many institutions, both for customer acquisition and retention.

But the factors that matter more are, if anything, an even bigger stretch for the traditional banking business model and culture. Probably the most profound and far-reaching is consumers’ oft-stated desire for simplification, customization, control, and enjoyment—which will affect everything from what the bank offers to how it operates.

Better customer experience must begin with the bank’s products and services. Too often, today’s bank customers face dozens of choices, often involving minor distinctions whose only real effect is to waste the customer’s time. And in some markets, complex products led to accusations of “hidden” fees that could catch customers by surprise—leading some (even among the affluent) to abandon bank accounts for alternatives such as prepaid cards.

Yet customers still want to make sure that products really do fit their needs; more generally, they want room to customize the banking experience. Several digital-leader banks have responded by introducing online platforms that let consumers customize a few basic product features. For credit cards, consumers can choose different designs and payment terms: for mortgages, they can designate a “payment holiday month.”

Increasingly, banks are turning to leading companies in other consumer industries for ideas to improve customer experience. Echoing online retailers, Bankinter introduced its “Comparator” price-comparison engine for financial-services products. The bank took a calculated risk that the benefit of meeting customers’ needs for objective, transparent information would outweigh any lost sales to competitors.

Taking a page from the consumer-electronics industry, BBVA engaged leading design firm IDEO to “humanize” and “Apple-ize” the ATM in ways both small (making sure the bill denominations shown on the screen match the actual cash dispensed) and large (incorporating software that rearranges the welcome screen to highlight the user’s most common transactions). After winning the 2011 silver award from one of the world’s leading international design competitions, the “ABIL ATM” is now in production and being rolled out across BBVA’s network.

Crossing the channel

As mobile, cloud-based, and smart device technologies mature, channels that were once separate are now blending together. New branch concepts, such as Citibank's new "smart banking" location in central Tokyo, are supported by advanced interactive and user-friendly remote-access technologies. As a result, branches can become less transactional and more service oriented.

Conversely, remote-channel designs must become simpler so that customers can handle both the basic transactions that no longer require a branch visit and the additional technology-based services that offer more value. Some institutions are starting almost from scratch, ridding their Web sites of opaque banking jargon in favor of intuitive phrases such as "my bills," "saving for my trip," or "my house fund." That gives customers the control over their finances that so many are asking for.

As consumers take advantage of these multichannel opportunities, they place an even higher premium on consistency. Institutions must therefore ensure that regardless of whether the customer is using a branch, a Web site, or a mobile application, the core content and presentation should be as close to seamless as possible. (See the section "Reaching the ideal: The seamless customer experience," in Chapter 3, "Is the branch obsolete in a multichannel world?")

Tight integration is important not only for customer convenience but to aid in the more urgent goal of increasing cross sales. Consider the customer who starts a mortgage application online but stops partway through. At some banks, if the customer later tries to complete the process while visiting a branch, she may discover that the in-person application is very different from the one she started on her computer. That experience alone could easily alienate her permanently. By contrast, leading banks install systems that can detect when a consumer has abandoned an application, save it automatically, and send a message to the call center to follow up with an offer of assistance. Again, the medium should be platform agnostic: the customer may want to speak in person, via e-mail, or just ask to be directed to the right mobile or Web sign-up page.

Better promises via lean processes

That sort of seamless transfer reflects the way consumers increasingly behave: as if there are no boundaries between once-distinct concepts such as call centers, online banking, ATMs, or in-person locations. But erasing these long-standing distinctions puts a serious strain on process design.

Greater automation, particularly in tandem with a larger “lean” redesign, enables the type of straight-through processing that has the largest impact, but it will of course require its own investment. The reward, however, can be substantial: institutions that have made these commitments have been able to make entirely new competitive promises to their customers. For example, Activobank introduced a “20 minute rule”: from the moment the customer decides to open an account, the entire opening process can take no more than 20 minutes of the customer’s time. That 20-minute period is enough for scanning ID and compliance documents, running credit scores, producing fully activated debit and credit cards, and using the ATM to print checkbooks and set up all logins and passwords.

Creating capabilities

The above examples highlight several areas where banks will need to strengthen existing infrastructure, or even develop entirely new skills.

Investing in IT. Although banks have long been among the most voracious consumers of technology, launching a multichannel, digital-centric platform will necessitate whole additional classes of IT investment. Robust core banking systems must move beyond basic transactional and risk-management functions to accommodate advanced customization and straight-through processing. And they must support the big data and analytics needed in order for cross-selling offers to be relevant and timely.

Building on “big data.” Yet the sheer quantity of data that banks will be able to see and integrate could allow them to leapfrog leading retailers. The big-data capabilities that a leading European bank recently implemented allow it to track its credit-card customers’ real-time purchasing behaviors, covering the categories purchased and their sequence down to the customer and street level. Credit-card customers who opt in for location-based services can receive targeted coupons based on how they last used their cards: a customer buying women’s shoes might get a discount from a nearby dress shop.

Embracing new marketing frontiers. Digital-marketing and social-network capabilities thus represent a new frontier for an industry that has traditionally lagged behind other consumer-oriented sectors. Some cutting-edge banks are moving even further, integrating banking capabilities directly into the social networks themselves. Alior Bank, Poland’s first digital-centric bank, has developed a Facebook application that ties into the bank’s most popular Web site. Clients can directly transfer money to a profile on Facebook with the help of the “Alior Payment” app, which includes a special bank account

accessible for Facebook transfers. Users can complete these transfers without leaving the Facebook page or logging in to the bank's Internet channel; for security, the app provides both a captcha box and a one-time transaction-specific SMS password. The only additional requirement is that the recipient must also use the same Facebook application, which involves simply filling in a short registration form. Thereafter, users can transfer the money to any domestic bank account.

Partnering beyond banking. And that highlights the last piece of the puzzle: managing partnerships. Banks operating in the digital world will need to cooperate with a far greater range of stakeholders than they did in the past, ranging from IT providers to mobile companies to local retailers. Activobank recently teamed up with Vodafone to offer attractively priced iPads and iPhones as the welcoming offer. A large Chinese bank is working with leading online-gaming companies to offer free games in a mobile-app store to customers who maintain multiple product relationships.

Prudent experimentation

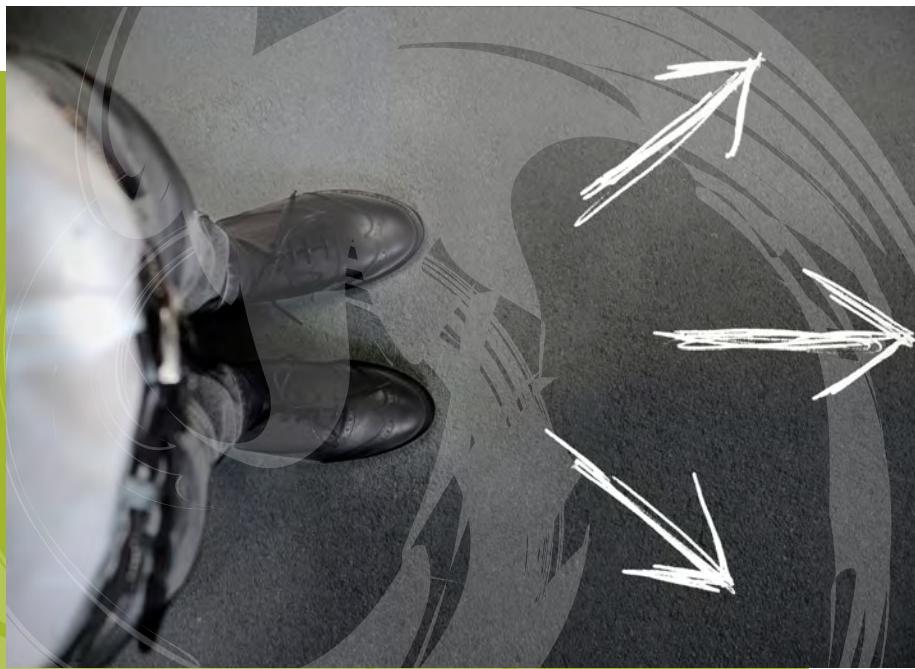
Making just one of these changes is difficult. But banks that decide to address all four must also address a deeper, cultural barrier: perfectionism and intolerance for failure. In the wake of the global economic crisis, it's understandable that even institutions that avoided the worst dangers would now emphasize the tried-and-true, refining and re-refining every new idea before releasing it to the market.

But technological forces alone suggest that this conservatism could quickly become downright risky, as it leaves an institution exposed to innovative attacks from unseen quarters. Instead, banks must allow for prudent experimentation, testing ideas in small-scale pilots that provide ample room for adjustment. That may mean changing incentives, organization structures, and management targets so people feel freer to collaborate and try new ideas, even when they do not work the first time. And senior management must reinforce the message that an industry in flux will need innovation to survive. To support this change, industry leaders such as BBVA, La Caixa, and Citibank have created independent innovation centers and even corporate venture funds to incubate emerging ideas and business models.



For banks in Asia, digital innovation provides an avenue for harnessing some of the world's fastest growth, in the world's largest markets, with the world's most advanced technologies. Getting there will not be easy. But leaders should consider this question: if compelling digital platforms helped banks in developed countries increase new digital-centric customer acquisition and wallet share by an order of magnitude, what could they do in a market where the Y-generation and new middle classes are expanding and GDP is growing at 5, 8, or 12 percent per year?

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Chapter 3

Is the branch obsolete in a multichannel world?

Jiab Chusacultanachai and Kiyoshi Miura

Key highlights of this article:

- Multichannel banking is coming of age; banks are at last starting to see earnings from all the new channels they have created.
- In many parts of Asia the branch will continue to play a vital role for some key customer segments, especially in sales and as a touch point for information.
- New formats are essential for the branch to fulfill its new role.
- After a careful assessment, the network can usually be trimmed; some branches can go, and staffing can be reallocated to provide greater expertise to customers.
- For the branch to continue to be relevant, the bank must provide customers with an utterly seamless experience, in which information, transaction quality, and communications are identical in every channel.

The branch is not going away, but it will never be the same. Here's how Asia's banks can get in step with multichannel banking—and get the most out of their still-valuable branch network.

Multichannel banking is not new, but making profits from multichannel is very new indeed. The past 15 years have seen several new channels emerge—the Web, the smartphone app, the call center. Each of these has added considerably to customers' convenience, but for banks, each channel has presented problems and added costs, without much compensation in the form of additional revenues or profits.

Today, multichannel is moving into a new phase, in which customers reap even greater benefits, and banks earn additional profits. In McKinsey's 2011 survey of multichannel behavior in the Netherlands, we found that on average multichannel customers take more products than others—nine, as opposed to six for customers that use two channels, and five for customers that use a single channel.

Accordingly, the revenue they generate for the bank is substantially higher; multichannel users produce 110 percent more than single-channel customers. And multichannel users, with their reverence for browser- and app-based banking, are much more loyal than branch-only users; the time invested by the customer to customize his online experience makes the relationship very "sticky."

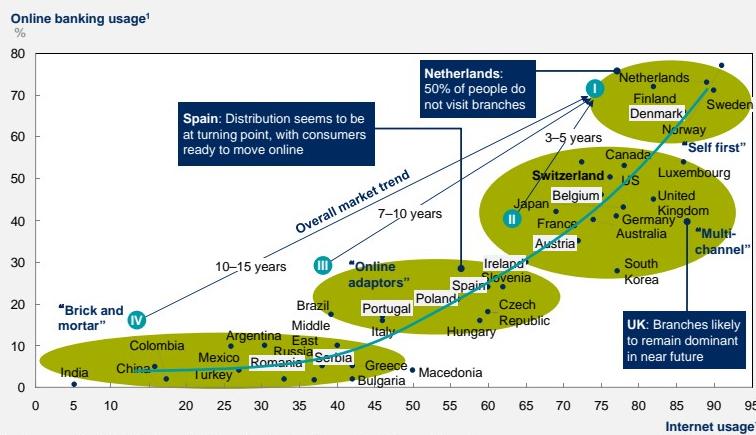
Additional revenues are a big part of the new profits from multichannel; but so too are steps to lower costs in thoughtful ways. In this article we explore the changes that multichannel has brought to banking, and in particular the effects on the branch and its role, as well as the steps that banks can take to prepare the branch network for multichannel.

Why multichannel? Why now?

Everyone is well aware that the Internet is reshaping retail banking. But not everyone knows just how far some markets have come, and how far others have to go. McKinsey research finds that Internet banking usage in some markets in Scandinavia is almost universal, while other emerging markets are just getting started (Exhibit 1). In fact, we see the world's banking markets settling into four clusters: those such as Norway and Sweden, in which customers essentially serve themselves through online channels; those in which customers use many channels to bank, such as the United States and the United Kingdom; those in which online usage is on the steep part of the rising curve, such as Spain and Poland; and those that are still almost entirely focused on traditional branches.

Exhibit 1

Internet usage and online-banking penetration go hand in hand.



In many of these countries, especially those in the second and third group, the pace of change is sharply accelerating, driven by the spread of computers, broadband connections, and smartphones. The shift online can also be seen quite vividly in the rapid decline in the number of branches. In the Netherlands, for example, we studied four big banks with a total of 5,054 branches in 2000; by June 2011, the banks had cut their networks to 2,459 branches. One of the banks halved the number of its branches over this period.

By and large, Asia has not yet jumped on this trend toward multichannel banking. With the notable exceptions of some small markets such as Singapore and Hong Kong, most Asian banking markets, especially India and China, are still characterized by the bricks and mortar of the traditional branch and ATM. South Korea's banks are expanding briskly.

However, we see strong signals of impending change. In McKinsey's 2011 personal-finance survey of Asia, a biennial research program begun in 1998, we saw for the first time a decline in the use of branches and growth in the use of new channels such as online and mobile. In Asia's developed markets, branch usage fell by 29 percent from 2009 to 2011; emerging markets saw a similar decline. Meantime Internet and mobile banking shot up, by 36 percent in developed markets and 39 percent in emerging markets.

The still-valuable branch

Internet and mobile can and should become real profit generators for Asian banks, as our colleagues discuss on page 9 (see "Chapter 2: Digital banking in Asia"). But what about the branch? Will Asia's consumers gravitate online like Scandinavians have done? Should Asian banks call their property agents and start to sell off prime branch locations?

The answer, as always in Asia, will vary considerably from market to market. In much of emerging Asia (especially India, China, and Indonesia) urbanization will likely continue to drive enormous expansion of branch networks. New banking markets are being created each year by the influx of huge numbers of people; banks must provide coverage through the branch. Regulation can sometimes make it difficult for banks to build branches, and it usually makes it even harder to close them. In these markets, the efficiencies of multichannel usage will be masked for some time by the growth of branch networks. In parts of developed Asia, labor laws can sometimes keep banks from closing branches as quickly as they would if they were to base channel decisions purely on economics.

How will these forces—the rise of multichannel usage in consumers, the uniquely Asian characteristics of big consumer markets—play out? Only time will tell, but it seems clear already that some markets (Australia, Hong Kong, Japan, Singapore, perhaps South Korea) will soon reach the “self-service” model, while others (China, India, Indonesia) are nearing the steepest part of the curve, when multichannel usage takes off exponentially. Even in those markets where multichannel behavior is slowest to take off, the shift to direct channels will have banks pondering how to optimize their branch networks.

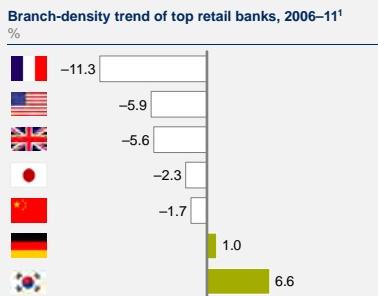
But they cannot move precipitately: there a lot of residual value inherent in the branch network. The branch will continue to be an important sales channel. In a 2010 McKinsey/European Financial Management and Marketing Association survey of European banks, executives said that 84 percent of current-account sales came through the branch, but they expected that to decline only to 53 percent by 2015. They held similar expectations for other key products: savings-account sales in the branch would decline from 77 percent to 38 percent; investments, from 78 percent to 58 percent; and consumer finance, from 73 percent to 32 percent. In all these cases, the branch will still drive a significant proportion of sales. In mortgages, expectations are even higher: banks expect to be selling 72 percent of all mortgages from the branch in future, down only slightly from 80 percent in 2010.

Further, some high-value customer segments tend to prefer branches. After analyzing their customer base, some leading multichannel banks have found that a portion of their high-net-worth customers, for example, prefer branch banking.

In short, it is a mistake to assume that as the shift to online banking gathers speed, the branch network must be radically trimmed. To be sure, some major markets such as France, the United Kingdom, and the United States have reduced branches in line with the trend (Exhibit 2). But in some markets where digital banking is well advanced, branch networks are holding steady (Japan), and even growing slightly (Germany and South Korea). And in countries where digital banking is just getting started, such as China, branches are in decline, though not as quickly as one might expect given China’s dramatic growth in mobile usage. In each case, changes in branch networks are heavily influenced by an array of factors, such as broader economic growth, urban density, regulation, and others. Bankers would do well to understand the particular economics of their markets before making broad-based decisions on the “right” size of the network.

Exhibit 2

Big banks in many markets have reduced branch density.



1 Average of major banks' additions and subtractions to branch networks, excluding effects of M&A

Source: Banks' public disclosures; McKinsey analysis

Branch banking's new role

Bankers must also understand precisely the value of the branch in their markets, which we argue will be driven by three variables: the makeup of the bank's customer base (and its preferences for branch banking), the bank's ability to use the branch as a touch point to trigger multichannel sales, and the branch's utility as a source of information to customers.

Banks should invest in a customer-segmentation analysis, to find out which customers use each channel, which customers use several channels, and how they think about each channel (Exhibit 3). They may well find that some branches serve a disproportionate number of affluent, investment-oriented customers—and not just those branches in the expected wealthy neighborhoods. Another likely finding: many customers of all stripes like to visit a branch on their commute to work, to get information on a product or to open an account. The same customers may never visit the branches closest to their home.

At the same time, banks can dig into the costs of each customer group.

Obviously, people who insist on using branches and the contact center are more expensive to serve than those who only use the bank's mobile app. But there are shades of variation within these broad principles, and banks should establish as accurately as possible the costs of each segment, and many subsegments as well.

An understanding of segments and the cost to serve each segment will provide most of the foundation for considered decisions about the branch network, but banks should not overlook the extent to which branches serve as a touch point for multichannel sales. At a minimum, banks will need to investigate

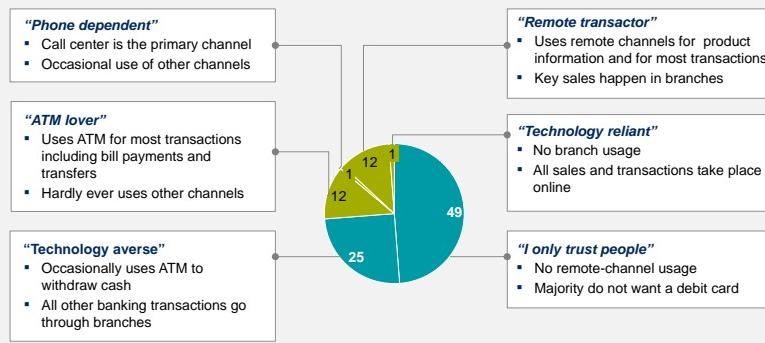
the connections between branches and other channels to ensure that the links between channels—especially between telephone and branch and Internet and branch—are strong. Follow-up phone calls and e-mails after branch visits are a must. Other sorts of links, such as using direct-marketing tools to lure customers to the branch to provide more personalized information, can also serve as a powerful influence in the customer's decision-making process.

Exhibit 3

Banks should understand the differences among their customers.

Typical customer base for a major Asian bank

% of total transaction volume



Finally, the branch has a vital role to play in the distribution of information. McKinsey research has established that the purchase process is no longer a straight line: it is a winding consumer decision journey, as customers gather information in many ways and places, and feedback loops shape their thinking at every step.³ As customer decision making becomes more complex and takes place in more channels, the branch becomes more vital. It may have lost part of its edge and monopoly as a point of sale, but its role as a critical information channel continues.

Getting the branch ready for multichannel

To take advantage of the shift to multichannel, retail banks should consider changes to four aspects of the branch: locations and format, network density, staff size, and staff expertise (Exhibit 4).

³ For an introduction, see "The consumer decision journey," mckinseyquarterly.com, June 2009.

Exhibit 4

Four critical levers can improve the branch network.

EXAMPLE

New location and format

- New "store-like" outlets provide
- Open spaces
 - Tablets available for customers

Staffing: Capabilities

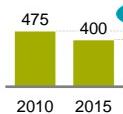
Radical shift from teller and back-office service ...



... to sales and advice

**Decrease in branch density**

Branches per million inhabitants



-16%

Can be as high as 30–40% in some countries

Staffing: QuantityAverage FTE¹ per branch

-33%

- Fewer FTEs needed as lower-value activities move to remote channels
- Mix of people and skills can be changed

1 Full-time equivalent.

New locations and formats

Branch architecture is continually evolving, and the latest shifts reflect the broader trend toward multichannel. Banks can catch busy customers with new outlets near shopping, work, and on the transport links between home and office. Many branches are becoming more store-like, and are even aspiring to provide open space for customers to relax, check messages, read, and talk. Tablet computers for the public can help with this, and can also help provide information.

Many of these new formats are designed to meet the needs of specific customer segments. For example, a Japanese bank is designing a new format for locations in high-income areas, with expanded space for consultations, a more welcoming reception area, and a sleek design meant to convey tranquility and transparency. Another has opened a salon on a high floor of an office tower, from which it provides services to wealthy customers at their workplace. Some banks are experimenting with ways to reach female customers, by employing all-female staff. Citibank in Singapore has opened some "super-lean" branches in shopping malls—essentially, glassed-in kiosks with one or two bankers on staff.

The full-service branch continues, of course, but with a new emphasis on the customer experience. Citibank's new architecture includes a wall of video screens, so that customers can check general and business news; interactive planning tables with touch screens built into the tabletop; workspaces for

customers; and tables to consult with bankers, either in person or using Facetime. Even the ATM lobby is improved, with 24/7 video access to service experts.

Branch density

As banks build new, small, shoplike branches, they will also want to close some older branches that are being left behind by the shift to multichannel. To figure out which ones, banks can do simple analyses of traffic; year-on-year patterns may show secular declines. But these declines can sometimes take years to show up, so leading banks are using other techniques. Analysis of customer segments can reveal how far each group is willing to travel to use a branch, a trait that can be adjusted for urban, suburban, and rural locations. Customers' willingness to travel also turns out to be greater for some transactions. A detailed analysis of the micromarket served by each branch can gauge the size of a branch's likely customer base after multichannel shifts take effect and the number of customers who might transfer their business to other nearby branches.

Staffing size

To be ready for multichannel, branches will also likely need fewer employees. Banks have big opportunities to make their branches "lean," thus making them more productive. One key analysis looks at the amount of time that tellers take to conduct basic transactions; surprisingly, many banks find an enormous disparity, of 50 to 100 percent, in the times recorded by tellers. Establishing standard procedures and training staff in them can drive productivity improvements of up to 7 percent. Another analysis looks at the peaks and valleys in demand, as measured by the length of the queue for tellers, and the staff that is on hand to cope. Typically, branches almost never have too few tellers, and usually have too many; one extra teller per branch is not uncommon. Banks can adjust staffing configurations and extract productivity gains through the use of schedule boards and other visual management techniques, which help workers shift seamlessly from one activity to another.

Staff expertise

Some of the savings in staff time and productivity should be redeployed, with a much greater emphasis on sales. At leading banks that have prepared for multichannel, branch staff now spend as much as 60 percent of their time on sales, up from an average of 20 to 30 percent. Not every banker finds it easy to make the shift, so banks have to be ready to help, with training that guides sales reps through the tricky "moments of truth"—the critical junctures in every transaction when banking relationships are forged. Reps will need

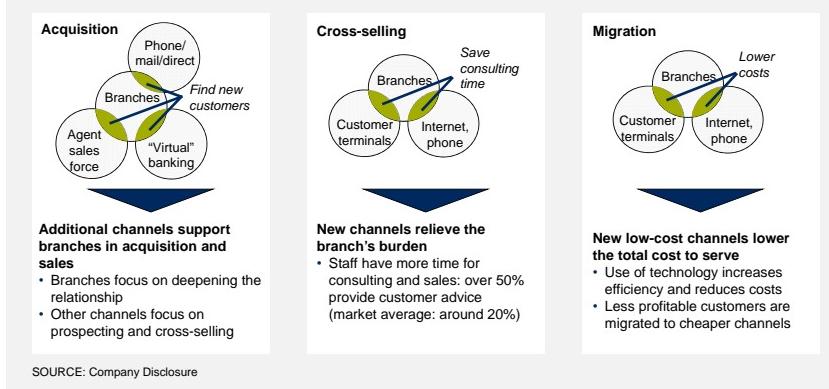
thorough assessments to understand any skill gaps they might have, and “forum and field” programs that use adult-learning principles to build those skills. Strong performance-management systems can make sure that reps stay on track.

Putting it all together

Two banks have shown some of the potential in rethinking the branch for multichannel. Spain's Bankinter has made many changes along these lines, and is now bringing the new channel architecture to bear in pursuit of three goals: customer acquisition, cross-selling, and migrating customers to the lowest-cost channel (Exhibit 5). In acquisition, new channels can help pick up the slack from branches. To improve cross-selling, a true multichannel experience can create more time for staff to sell. And by encouraging some customer segments to move to lower-cost channels, banks can maintain a good experience while reducing their expenses. In 1993, 80 percent of Bankinter's transactions were made in the branch; in 2009 just 33 percent were, with the rest going through lower-cost channels.

Exhibit 5

Bankinter's multichannel approach has three benefits.



Conestoga is a community bank with 14 branches in Philadelphia. It has replaced the traditional teller line at one downtown branch with personal teller machines (PTMs), which are located inside the branch and provide a live video link to remotely located tellers. They can be configured to do almost all traditional branch transactions, including deposits, withdrawals, check cashing, money orders, cashier's checks, and so on. At scale (about 15 machines), a PTM system can support multiple branches; one remote teller is needed to support every

three PTMs. Conestoga also provides customers with a conference room where they can videoconference with product specialists and advisers. Apart from the productivity savings, Conestoga also reckons that the new technology will help it access a younger cohort of customers.

Reaching the ideal: The seamless customer experience

As they design the right branch architecture to reach their most desirable customers, boost revenues, and lower costs, banks need to think about the connections between the branch and other channels—indeed, the connections among all the channels. Some channels predominate at a certain point of the purchase process, but no channel is so little used that it can safely be ignored. That is especially true in after-sales service, where customers like to use any and all channels to conduct transactions, check balances, receive alerts, and so on. (In short, banks must seek to provide “multichannel hoppers” with the ideal experience—a strategy our colleagues discuss on page 12.)

These patterns are drawn from an analysis of many customers of all types; the contact behaviors of customer segments will vary widely. Customers who prefer self-service may never visit the branch, and people who put a lot of stock in personal trust may never use a mobile app. But most segments will touch several channels. Banks have to capitalize on those behaviors, because it is precisely these customers that produce the most value for banks.

A good first step for many banks is to assess the current customer experience, looking for places and events where the bank is letting customers down, leading to customer “leakage.” For example, in the call center, an assessment might reveal that customers abandon their calls too frequently, or that contact specialists lack the support needed to follow up on conversations that suggest customers need a particular product. A review of ATMs might show that paying bills is needlessly complex, or that check imaging could be economically expanded to more machines. Some banks’ Web sites don’t offer live chat, an obvious value-adding feature that would be readily revealed through a comprehensive assessment.

Once the gaps are known, it is a fairly simple matter to figure out which ones lead to the most leakage, and remedy them. One good example of a seamless multichannel experience can be found at Nordea, the big Northern European bank. It is rolling out a new mortgage-underwriting process that relies heavily on digital documentation. No matter the channel, the customer will complete a quick digital document to seek approval. Digital signatures speed the document through the process. Connections with property registries

are automated, as are payouts, once collateral has been fully established and verified. Archives are also digitized.

That new process will also mean a new customer experience. Much of the somewhat tedious work in which bankers help customers enter data will disappear; customers will be able to enter their own data, supplemented by automatic feeds from other sources. The banker will be free to focus on advising the customer on the best product for his or her needs.



Building a successful multichannel architecture is not a trivial undertaking. But banks can accomplish much of the work in about nine months with a three-step program. First, they should understand the extent to which they can leverage their current assets to appeal to customers; typically, much of the network can be easily repurposed in ways that drive customer satisfaction and drive productivity within the channel. Next, they can add some capabilities to the branch that will both increase productivity and, again, boost satisfaction. At this stage there will likely be a need to revamp specific capabilities in people and technology, targeting critical multichannel intersections, for example, from the branch to the Internet or from the call center to the branch. As a third step, banks can then design the channel integration needed to provide a seamless experience.

The process will inevitably force the bank to become more multichannel in its decision making. For example, banks will need to set up mechanisms to monitor customer activity across channels and put in place joint key performance indicators to monitor progress. Product and channel teams will have to decide jointly on investments where both the costs and benefits cut across channels. The shift of gravity from the individual channels to a more collaborative platform of multichannel decision making is perhaps the biggest challenge for banks to manage. Only those banks that master the formula will be in position to capture the prize.

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Chapter 4

Creating the customer-centric retail bank

Fabian Hieronimus and Christian Roland

Key highlights of this article:

- In Asia, customer centricity is a much talked about term, but many banks have not yet been able to fully turn the vague concept into something that is concrete and linked to impact
- From our experience, there are three specific archetypes of customer-centric business models that can help anchor a bank's effort on this, making it much more impact-focused
- Archetype 1: Relationship champions – focus on building deep relationships with selected sub-segments
- Archetype 2: Customer-service champions – emphasize excellent service delivery across all customer touch points
- Archetype 3: Convenience champions – strive to make banking as easy as possible for customers

Banks around the world are trying to reshape their business models to become more customer-centric. In this article, we explore why customer centricity matters for banks in Asia, outline three archetypes of customer-centric models in retail banking, and describe the requirements for successful implementation.

In the aftermath of the financial crisis, banks worldwide say they are increasingly focusing on making the customer the center of their business models. This may be a belated acknowledgement by banking executives that they could no longer develop, sell, and service products without a deeper understanding of their customers' needs.

The idea of a customer-centric banking organization has been around for a long time; indeed, most financial institutions would contend that they have always paid attention to customers. But being a customer-centric bank means more than greeting savers at the door—it's a deeper level of engagement than most banks, particularly in Asia, have been willing to offer. Many banks there

have resisted committing to real customer centricity because their strong growth rates and profits have undermined the case for making big changes and tough choices. They may no longer have that luxury.

Two factors could push Asian banks toward a stronger customer orientation. First, despite heavy investments in their channel networks and improved product offerings, holdings per customer remain low in many banks. Second, customer expectations for service levels, advisory quality, and integration of channels are rising. As a result, overall customer loyalty is decreasing in many markets. In sum, Asian banking customers are saying they want more than a transactional relationship with their banks.

Can Asian banks overcome organizational inertia and move to a true—and profitable—customer-centric model? Our research shows that many banks in Asia and elsewhere have tried to shift in this direction, but results have been disappointing. In this article, we identify three archetypes of customer-centric business models that have succeeded and discuss what Asian banks can do to start the journey to customer centricity. McKinsey experience and research show that a customer-centric business model leads to greater loyalty, higher cross-selling, and lower customer attrition, all leading to more revenue and profits.

What customer centricity is and why it matters

What distinguishes a customer-centric bank from others? In our definition, a customer-centric model is based on a deep understanding of customer needs, with channels, processes, and products tailored to meet the needs of different segments (Exhibit 1). A customer-centric model differs from a channel- or product-centric model: in the latter two cases, customers are “owned” by the units that acquire them, and the customer experience is optimized for a particular channel or product, rather than across the full range of channels or products. In a product-centric model, for example, the credit-card division would enroll customers through a credit-card-specific form, try to optimize use through card-specific marketing campaigns, and increase loyalty through a bonus program based on card use. In a customer-centric model, customers who wanted to open an account would work with bank staff to identify their needs and complete a single application form for multiple products, while the loyalty program would take the full customer relationship with the bank into account.

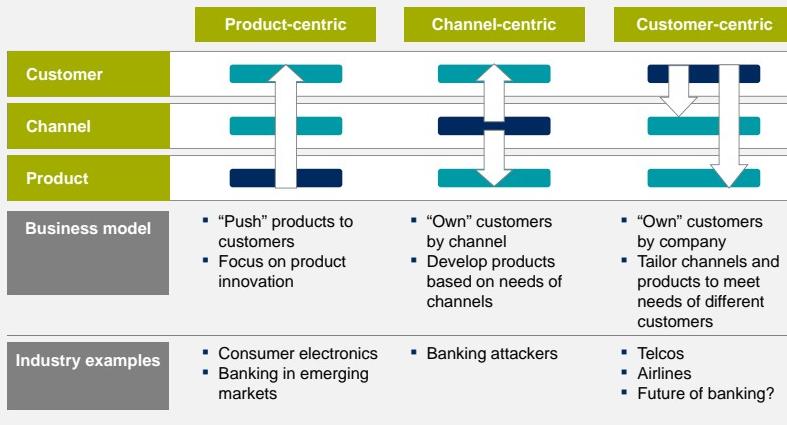
In emerging Asia,⁴ most banks are product- or channel-centric. While they would argue that they focus on the customer, there is clearly room for deeper

4 Emerging Asia comprises China, India, Indonesia, Malaysia, Thailand, the Philippines, and Vietnam.

engagement: McKinsey's Asia-wide survey on personal financial services showed that product holdings per customer remain low and customer loyalty in many markets is declining.⁵

Exhibit 1

A customer-centric business model is based on a deep understanding of customer needs.



Our research found four important changes in customer behavior and expectations across Asia (Exhibit 2):

- Loyalty drivers are shifting. While price and accessibility of branches and ATMs were once the biggest concerns of customers, they are now table stakes. Quality of service and staff is becoming much more important.
- Use of multiple banking channels—branches, ATMs, online, and mobile banking—has become a reality for Asian consumers. This increases the demand for seamless information flows across those channels.
- More than 60 percent of emerging Asia's consumers would prefer to consolidate relationships if a bank is able to offer seamless service.
- Consumers show decreasing loyalty to their financial institutions.⁶

⁵ In 2011, McKinsey surveyed 20,000 customers in 13 Asian markets about their personal-financial-services behavior. In Southeast Asia, for example, product holding for primary banks stands at 2 products and for secondary banks at 1.1 products.

⁶ Despite overall high satisfaction with their banks (80 percent of customers across Southeast Asia agree or fully agree that they are satisfied), there is significantly lower willingness to recommend the bank to a friend or colleague (only 30 percent in Singapore, 54 percent in Indonesia, and 60 percent in Thailand would be willing to recommend their bank).

Exhibit 2

There are several important shifts in consumer behavior across Asia.



1 Emerging Asia comprises China, India, Indonesia, Malaysia, Thailand, the Philippines, and Vietnam.

Source: McKinsey customer decision journey/multichannel survey, 2011; McKinsey personal-financial-services survey, 2011

How can banks build a customer-centric model around these changes? Banks must first understand what matters most to banking customers. Our research identified topics that are top of mind in the region—obviously, not all of the following factors are equally important. Banks should try to understand which of the levers matter for their target customer base and pick one or two areas in which they want to excel.

Service orientation. Banks should provide outstanding service and rarely make mistakes; if they happen, they should be resolved quickly.

Convenience orientation. Banks should have branches and ATMs that are easy to reach, provide a broad range of channels for 24/7 banking, and offer straightforward account-opening procedures.

Customer orientation. Banks should be flexible in their dealings with customers and willing to go beyond standard procedures, be knowledgeable about products and services, and give customers the feeling that what they receive is unique.

Pricing orientation. Banks should offer low fees and charges for services, as well as attractive interest rates on deposits and loans.

Relationship orientation. Banks should encourage the development of trust-based relationships with some employees and reward customers that have longer and deeper relationships with their institution. In many markets in Asia, we are seeing that pricing and basic service are becoming less important as differentiating factors, while customer and relationship orientation are becoming increasingly significant.

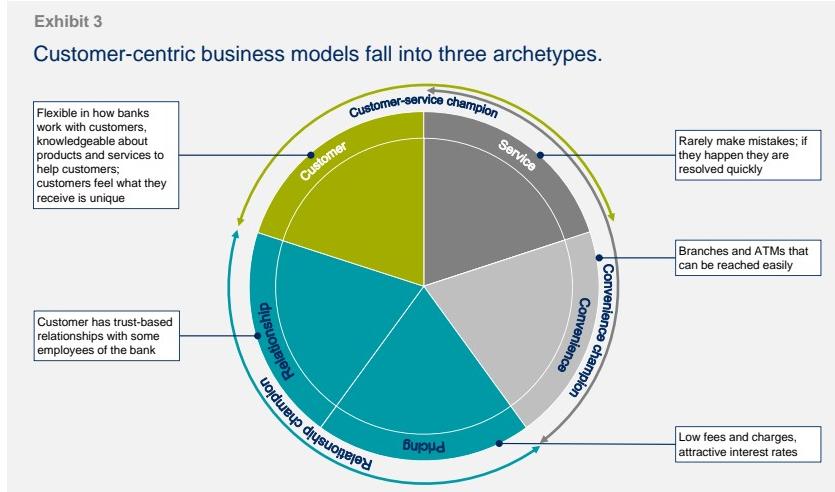
Toward a customer-centric model

These five factors are key to winning customers' hearts and minds. However, banks must avoid trying to be everything to everyone. There are clear trade-offs among some of the factors, and their relative importance differs by market⁷ based on customer preferences and the competitive situation. The starting position, strengths, and capabilities of each bank also will influence the choice of the most relevant factors.

In our work, we have seen the factors noted earlier—service orientation, convenience orientation, pricing orientation, customer orientation, and relationship orientation—translate into three archetypes of successful customer-centric business models (Exhibit 3). The boundaries of the archetypes overlap to a certain degree, and banks may choose to pick elements from more than one archetype.

Exhibit 3

Customer-centric business models fall into three archetypes.



⁷ In broad terms, we are seeing a trend across Asia from “hard factors” to “soft factors”: the size of the branch and ATM network, as well as low prices, matter less, while service excellence and strong advice are at a premium.

Relationship champion

The basis of this archetype is building deep relationships with selected subsegments such as young people who have taken a job for the first time or affluent pre-retirees. Financial institutions that follow this path aspire to having customers say, "My bank really understands my needs and has solutions that fit. They are rewarding me for banking more with them."

In this archetype, banks focus on offering products that cover a majority of the needs of the relevant customer segment. So, in the case of an affluent pre-retiree, a bank might offer a package comprising savings and protection elements through insurance. Such a customer might also receive more attractive pricing for being with the bank longer and keeping more assets with it. To address customer expectations in this archetype, banks should invest in training for their relationship managers, customer-relationship-management systems that help the front line guide the customer to appropriate products, and product development based on deep insight into target segments.

How should bankers measure success for this archetype? They should look at the customer market share, how much of a customer's assets the bank holds, and the number of products held per customer.

If a bank pursues this model, it should avoid offering too many product solutions for ever-smaller sub-segments and seek to align the product pricing with true customer value (for example, taking care not to give steep discounts for certain segments). Otherwise, the cost of providing the products might spiral out of control, while the expected revenue may not materialize.

We see banks trying to become relationship champions in many Asian markets, but successes are still few and far between. Some multinationals focusing on affluent customers are further ahead, but often customers use them as secondary banks for their investments or mortgages, not as primary banks for all daily transactions and banking needs.

Customer-service champion

Excellent service delivery is the hallmark of this archetype. A successful application of this business model would prompt customers to say, "The employees of your bank really go out of their way to make things happen for me." The areas to focus on are service delivery in all channels, including fast and consistent responses to customer requests and speedy complaint resolution in the event expectations cannot be met. To make this happen, empowering frontline employees to take initiative is key. Banks may not go as

far as leaders in the service industry, such as the Ritz-Carlton hotels that give each employee a sizable budget to resolve a complaint or to delight a customer. But giving employees the ability to make decisions on behalf of the customer on the spot will go a long way. In addition, banks need to review and streamline their service processes to reduce turnaround time and errors.

The measures of success for this archetype typically are customer satisfaction and willingness to recommend the bank, as well as performance on operational indicators such as wait time in branches or call centers, errors per transaction, and speed of customer issue resolution.

Major pitfalls to avoid are undifferentiated service levels—priority customers should feel the difference, and higher-value customers should receive priority treatment.

An example of this archetype is Metro Bank, the first High Street banking launch in the United Kingdom in more than 100 years. Metro Bank emphasizes its service proposition over products and pricing. For example, it was the only bank in the United Kingdom to offer seven-day branch banking; it promised to end “stupid bank rules” to deliver quick, informal, and efficient service; and it gave access to free coin-counting machines and dispensers that noncustomers can use as well.

Convenience champion

The third archetype aspires to make banking as easy as possible for customers. Success would be if customers say, “My bank makes banking effortless for me” or “Banking is painful, but my bank has managed to make banking really easy.”

Key elements of focus should be the channels, the product-purchase process, and operations. The channels should be easily accessible (both with regard to proximity and opening hours) and well linked to ensure a seamless flow of information. Product purchases and service transactions should be as simple as possible—for instance, existing customers shouldn’t have to fill out detailed applications if they want to purchase an additional product. Strong operations should support delivery at the front line. One metric bankers should keep an eye on is the number of products held per customer, with a goal of “owning” all the customer’s banking needs.

A common mistake in this archetype is overinvesting in infrastructure (for example, too many branches and ATMs) and underinvesting in “soft” enablers like staff quality or collaboration among channels to ensure a seamless experience for customers.

An example of this archetype is the Malaysian bank Easy by RHB, which features a value proposition of “simple, accessible, and fast banking.” This player positions itself as a paperless community bank for mass-market customers; its branches are strategically located in high-traffic areas, and it has partnerships to open branches in grocery stores owned by a prominent foreign chain, at selected Malaysian post-office branches, and at light-rail transit locations. In addition to the branch channel, bank customers can get bill-payment and mobile-phone and PayPal account top-ups through mobile and Internet banking. Easy by RHB offers simple products on the spot with 10-minute approval time, even for personal loans.

The path to impact

McKinsey experience shows that a customer-centric business model can improve loyalty, increase product sales by 5 to 20 percent, and lower customer attrition by three to five percentage points. How can retail banks get started? Below, we lay out the journey. However, some of the steps, particularly in the later stages, may be taken in parallel.

Assess starting position and choose an archetype

Retail banks should begin their customer-centricity journey by looking at their starting position through a customer and competitor lens. To do so, executives should try to answer the following questions:

- What are the most important decision factors—convenience, service, pricing, customer orientation, and relationship—for a customer to start doing business with a bank and then deepen links?
- How do customers perceive our bank and main competitors on these dimensions? External market research can help answer this question; it might also be interesting to ask the staff at various levels in the organization the same question and compare external and internal perceptions.

Armed with research results, banks should then decide which customer-centric archetype fits best. The discussion in the top-management team should take into consideration not only the customer view but also the capabilities required to carry out the strategy. For example, even if customers say they value high-quality service as the main factor for choosing a bank, executives may decide against the customer-service archetype if there are already strong competitors in the marketplace or if they believe they can't build the internal processes to consistently deliver market-beating service levels. Once

executives agree on the archetype, they should translate it into a customer vision and promise that excites and guides the organization.

Customers at one East Asian bank, for example, were complaining that the bank's staff lacked a service mind-set, and the bank consistently scored lower than competitors on customer-service ratings. In response, the bank undertook detailed market research that revealed accurate handling of transactions at the branch was an important decision factor for customers. The bank's customers were twice as likely as competitors' customers to agree with the statement that staff made "mistakes once or twice." This helped the bank pinpoint where to make changes to its service aspiration and how big they should be.

Define the customer value proposition

Once executives choose an archetype, a bank should bring it to life by detailing the customer value proposition. A starting point is to think through what the customer would say is unique about the bank's offering and what it takes to deliver this. Doing so requires determining the main customer benefit, how the customer benefit compares with competitor offerings, and the reason the bank is able to deliver the benefit. For example, for a bank that aspires to be a relationship champion for selected subsegments, this could be, "Only if I bank with XYZ instead of A, B, or C (*main competitors*) will I get solutions that really fit my needs (*core benefit*) because Bank XYZ has a structured way to assess my needs, product solutions that are flexible in case my needs change, and knowledgeable advisers to help me (*reason*)."

Another Asian bank that aspired to build deeper customer relationships and thus increase product holding and share of wallet developed a two-part proposition: offering greater customer convenience in all channels and solving client problems rather than selling products. This proposition helped to focus the bank's transformation efforts on improving the service experience, particularly in branches, and investing in a needs-based advisory process and new product offerings.

There are two common errors to avoid when defining the customer value proposition:

- **Overpromising.** This may occur when a bank focuses on slogans, not changes in its operating model. It is easy to mistake a value proposition with the next marketing slogan. Many banks proudly state in their marketing communications that they are committed to building deep

relationships or say they will go out of their way in customer service. However, in a truly customer-centric model, banks must move beyond slogans and change the way products are sold or ensure greater consistency in customer service.

- **Overpaying.** In this case, offers don't match the economics of each segment. When designing a proposition and offering for a customer segment, it is easy to provide too many benefits, including price discounts, special promotions, and high service levels. Banks should look hard, particularly in the mass-market segment, to see if the cost of their product offering matches the expected profit from each customer.

Put the proposition and required enablers in place

Once the bank has defined the proposition, implementation can begin. Besides putting in place initiatives to bring the customer proposition to life, banks should also think through the broader set of enablers that will be required. This includes strengthening the marketing function to derive deeper customer insights, using an advanced business-intelligence and customer-relationship-management system to support the front line, and building up the operations backbone (Exhibit 4). In addition, banks should work on the specific enablers for each archetype, as described earlier.

When charting their journey, banks should try to avoid two common mistakes:

- **Overstretching.** This might occur when the executive responsible for looking after a customer segment lacks seniority and has limited authority compared with the product or distribution units. As a result, the segment view may not be taken appropriately into account when making decisions about product launches or distribution strategy. Banks can avoid this situation by ensuring that the segment leader has the appropriate seniority and decision-making authority.
- **Underpreparing.** This can happen when a bank insufficiently invests in capability building to get its staff ready for the new direction. Many of the changes in a customer-centric journey will ultimately affect the front line and operations. To facilitate change, banks should plan for significant investment in capability building. One Asian bank defined the required skills for each level of the frontline organization and then set up a program to train each level.

Exhibit 4

The three archetypes have common backbone elements.

	Relationship champion	Customer-service champion	Convenience champion
Customer insights	Strong marketing function for deep customer insights		
CRM ¹ /business intelligence		Advanced CRM system to capture customer information and support the front line	
Customer champions		Customer (or segment) champions in the organization that coordinate across product factories, distribution channels, and operations	
Operations backbone		Flexible yet robust operations backbone for fast and error-free delivery	

1 Customer-relationship management.

But when does a bank know it is on track and starting to create value? It is worthwhile to monitor metrics such as customer satisfaction, churn rate, and new money from existing customers at least on a quarterly basis. Banks can complement these measures with regular surveys of frontline staff—these employees typically have fine antennae to judge if the bank is really making progress and how customers are reacting to the changes.



Changing the business model from product- or channel-centric to customer-centric is no easy feat. Many retail banks in Asia still enjoy healthy growth rates and profits, so the case for change may not always be apparent. But Asian banking customers are demanding a different kind of relationship with financial institutions. Banks that fail to address this need risk losing market share and consumer relevance. In our experience, Asian banks that have aggressively pursued customer centricity have been amply rewarded in the marketplace.

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Chapter 5

Next-generation productivity improvement: Sales transformation 2.0

Akshay Alladi and Jatin Pant

Key highlights of this article:

- Leveraging technology can dramatically increase frontline sales productivity and transform sales-force management.
- Moving sales to direct channels makes it possible to target customers throughout their decision journey and reduces customer-acquisition costs.
- Harvesting analytics based on big data opens the way to generating new demand, including the use of customized campaigns and microtargeted sales.

To boost sales growth in the new market environment, retail financial institutions in Asia need a four-pronged strategy to leverage technology in the end-to-end sales process.

In Asia, retail financial institutions are confronted with significant challenges in the competitive landscape, including changing consumer behavior, technology disruptions, and a worsening macroeconomic environment. This is leading to significant pressure on revenue growth.

First, there is a notable decline in customer loyalty and an increasing tendency for consumers to hop across remote and physical channels and split their decision journey. Second, rapid advances in technology and related infrastructure (for example, mobile communications and big data) will cause greater competitive pressures, with newer players “leapfrogging” competition and levelling the playing field. Finally, an uncertain and volatile macroeconomic environment is affecting revenue growth and increasing potential risks.

Cranking up traditional sales-stimulation approaches will be insufficient to win in this context. Instead, retail financial institutions in Asia need a new

approach to overcome these challenges and boost revenues. They should take the lead by harnessing the potential of disruptive technology trends such as the immense popularity of smartphones and social media, the rise of big data, and cloud computing.

In this rapidly evolving environment, CEOs should answer four key questions:

- How can I dramatically increase my frontline sales productivity by leveraging technology?
- How can I move a significant portion of sales to direct channels in order to reach customers throughout their decision journey and reduce my cost of customer acquisition?
- How can I use smart analytics to generate demand and achieve microtargeting of sales?
- How do I get real-time and detailed information to assess the performance of my sales network at a granular level?

We recommend a technology-backed four-pronged approach to navigate the changing terrain. First, players will need a technology platform that provides new tools to enable the frontline sales force to increase its productivity. Second, a suite of direct-channel platforms should be used to better reach customers at lower cost. Third, a big-data analytics engine must be created to help generate new customer demand. Finally, companies should employ a technology-enabled system to improve performance management for the sales force. The four components can work in an integrated way to transform a company's performance, adding up to an innovative "Sales 2.0" model for retail banks.

What does the new approach look like? The traditional sales-stimulation approach relies on two elements: equipping the front line with tools and training that make the sales force more effective at engaging with customers, and managing the performance of the sales force based on regular (usually weekly) reviews. In a technology-driven environment, the effectiveness of both these elements can be enhanced significantly.

The "one size fits all" tools that the front line uses in the traditional approach can be transformed to have customer-specific offers and selling tools. Technology-enabled sales also helps identify the most valuable customers to target in the first place, dramatically increasing chances of conversion. In addition, technology enablement lowers the cost of acquiring and serving

customers. For performance management of the sales force, technology can again be harnessed to increase both the frequency and the granularity of performance management, leading to more insightful problem solving and root-cause analysis and driving greater accountability.

We have observed that best-practice companies that have implemented the approach have been able to significantly boost revenues and profitability within one to two years.

1. Boost frontline sales productivity

The front line presents the biggest opportunity to use technology for sales growth. Technology tools can simplify the task of sales agents, for example, making it possible to speed up the process and close leads faster. This can be achieved by using an integrated frontline technology platform that covers five areas.

The first area is a technology-enabled lead-generation system. This makes it possible to customize leads for individual clients and prepare personalized sales pitches. New leads generated in this way can then be delivered immediately to the salesperson via smartphone or tablet.

The second area is using technology to make the sales process more efficient. Greater efficiency can be delivered through the IT enablement of sales tools and techniques (such as frequently asked questions, product illustrations, and calculators for determining pricing), as well as through on-the-spot product and price customization. There is also scope to use technology to make customer service more efficient. Examples include displaying a detailed customer history and customized recommendations to resolve customer queries, and providing a video-chat facility to clients that makes available product experts and service staff.

The third area is using technology to make possible more rapid fulfillment of new business. Here, technology can facilitate automated approval and on-the-spot underwriting enabled by uploading and scanning of documents for instant approval. Technology also paves the way for new payment solutions using physical-swipe devices or payment gateways and for sales reporting by staff that provides actionable insights to the field sales force and managers.

The fourth area is using the platform for engaging with the frontline sales force. Examples of this kind of engagement include making it possible for employees to view rewards and recognition and to track their individual

performance in real time, as well as enabling collaboration across the front line—for example, using social networks to facilitate the exchange of best practices and other knowledge.

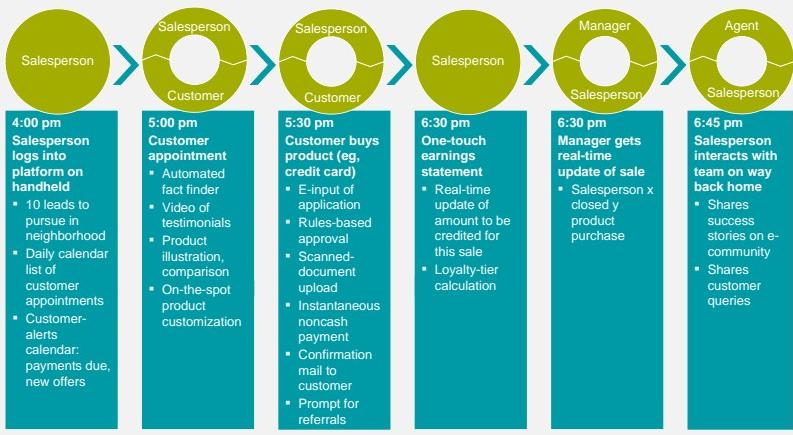
The last area where the frontline technology platform can be deployed is in training (see sidebar, “Capability building at scale,” page 55). Here, the platform can provide a knowledge center that houses resources such as e-learning chapters and refreshers.

This frontline technology platform has the potential to fundamentally alter the typical day in the life of a salesperson, making the sales process much quicker and more effective (Exhibit 1). Instead of taking several hours or even days to close a transaction with a customer, the transaction can be completed in two hours; lessons can be shared with colleagues immediately, and the salesperson will see the bonus she earned.

Exhibit 1

A frontline technology platform can profoundly affect the sales staff.

Tech-enabled agency ecosystem for agent



2. Increase customer reach and engagement through seamless multichannel integration

Customers are increasingly splitting their decision journey across physical and digital channels. To retain customers, retail banks have to integrate across these channels by developing a multichannel customer-acquisition process. This will fundamentally alter the way banks acquire and develop customer relationships—making possible broader and deeper reach, as well as greater

cross-sell and up-sell. It will also help to retain customer loyalties at a lower cost, since the cost to serve through direct channels is significantly lower.

Consider the following example of how the approach can play out between physical and direct (Exhibit 2). A customer calls a call center to inquire about mortgage products and provides the agent with information but eventually decides not to commit. When the customer later goes to get money from an ATM, however, he is provided with an option to schedule an appointment with a mortgage specialist, and this enticement leads the customer to the branch—where the mortgage specialist has prefilled application forms at the ready to start the process.

Putting in place four building blocks can enable companies to achieve physical-direct integration.

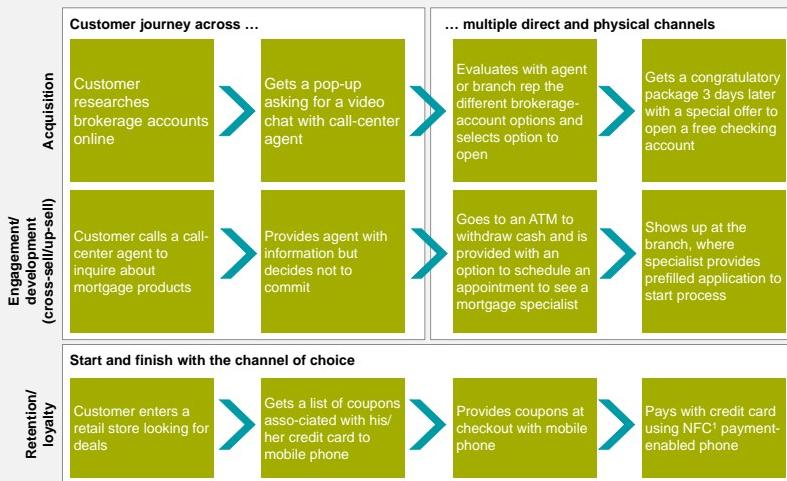
The first is digital demand generation, which makes it possible to generate additional leads for sales by using direct channels across multiple touch points—the Internet, mobile or tablet apps, ATMs, text messages, telephone, and interactive-voice-response communication modes. The second building block is smart tools, especially those that facilitate cross-selling and up-selling by accurately profiling customers and customizing the product offering based on those profiles. The third is putting in place intuitive product choices that enable a customer to select on his own the product that best serves his needs. The fourth is the use of direct channels for customer self-service, which reduces the cost of acquiring and serving the customer.

Using these direct-channel platforms can fundamentally alter the way that customers are acquired and the way relationships are deepened. The advantages of low-cost direct channels enable financial-services companies to expand their relationships with customers or add new customers, and this can translate to significant savings-per-new-customer-acquisition compared with traditional approaches.

The combination of direct and more traditional channels can provide substantial benefits to retail banks. For example, the integrated physical and digital sales-fulfilment model can deliver customer acquisitions at a rate that is 25 to 30 times faster than traditional branch-based sales models. An additional benefit is that implementation is relatively fast: our experience with banks across Asia suggests that this type of new customer-acquisition technology architecture, which integrates physical and digital channels, can be operationalized in a period of two to three months.

Exhibit 2

An example illustrates the multichannel customer-acquisition process.



3. Create a big-data analytics engine to generate demand

The big-data analytics engine can be harnessed not just to generate leads but also to design targeted and customized sales campaigns based on detailed profiling of customers. With big data, sales campaigns can be designed on the basis of potential (identifying the exact profile of customers who will be approached), expected hit rate (based on analysis of historical conversion rates for each customer profile), and expected bottom-line impact. Furthermore, big data allows banks to customize their sales approach. For instance, customers can be profiled on their preference history of responding to solicitations and then approached accordingly; one group might be approached via a direct mailing with a tailored offer (such as preapproved credit), while another group with a different preference profile could be approached with phone calls to schedule in-person meetings.

Creating such a customized system requires that banks structure their approach in a way that incorporates the following elements:

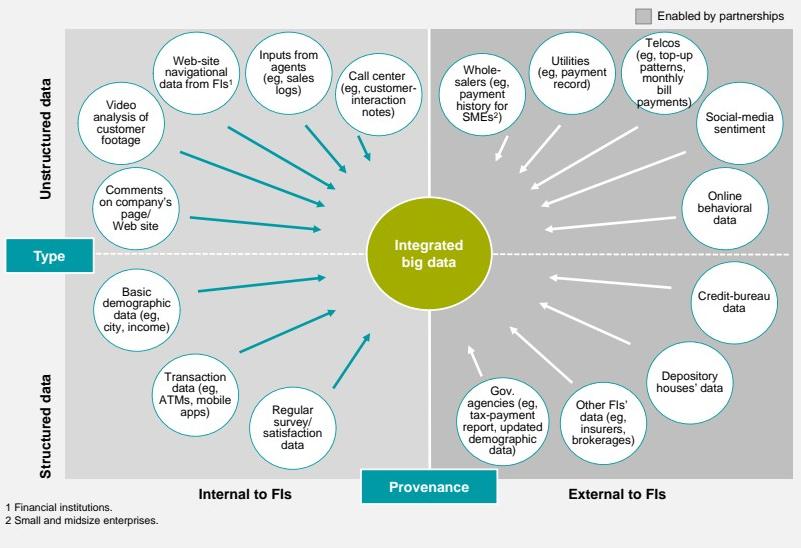
- **Access more data from internal and external sources.** Improving channel functionality and digitizing records can help to tap structured and unstructured data banks from internal sources. These include channel-

interaction data (for instance, call-center logs and cookies), demographic data, and transaction data. Banks can also source data through strategic partnerships with a variety of external sources, such as e-retail sites, social media, and credit bureaus.

- **Aggregate data for a single customer view.** Taking data from these multiple sources can be used to form a single and enriched view of the customer (Exhibit 3).
- **Create a robust analytics engine to design customized campaigns.** There are various types of sales campaigns that can be designed using analytics. These include propensity models that facilitate targeted cross-sell based on customer profiles (typically for products such as credit lines and credit cards or deposits and investments), event-based campaigns tied to customer-specific triggers (for example, product offerings timed to be communicated at the maturity of a loan, term deposit, or account cancellation), or new product bundles tailored to specific customer profiles (for instance, a preapproved loan offer might be included with newly linked accounts).
- **Feed customer data to all channels.** Before launching offers based on the engine's findings, it is important to feed customer data and "next best offers" (NBOs) simultaneously to all channels—both physical and direct—to ensure the offers made to the consumer are consistent.
- **Generate offers and prefill application forms.** Using the customer information it has acquired and in combination with real-time assessments of customer credit risk, the engine can generate real-time customer-level targeted offers and sales pitches. In addition, parts of product-application forms can be prefilled automatically based on data generated by the analytics engine.
- **Make campaign management robust.** Successful players ensure robust end-to-end campaign management by establishing "customer-lead-management factories." These factories are responsible for providing comprehensive information warehousing, managing offer engines and analytics, and coordinating campaigns across channels. They also conduct a rigorous cost-benefit analysis to gauge the effectiveness of the offers.

Exhibit 3

Data from multiple sources will inform a single customer view.



4. Manage sales performance in real time

The use of technology can also be extended for internal performance management of the organization's frontline sales staff. Since the front line now uses technology platforms for capturing customer and sales information, real-time performance monitoring at a granular level of detail is possible. Several retail financial-services companies in Asia have started using tablet-based applications to do this, enabling them to have more targeted performance dialogues and to identify root causes of underperformance.

Seeing the impact from technology-enabled sales

The impact of technology-enabled sales on the performance of retail financial-services companies can be massive. Based on our experience, for large incumbent banks (that is, those with annual revenues of between \$5 billion and \$10 billion, more than 2,000 branches, and over 10 million customers), the estimated impact on revenues is \$400 million to \$550 million, leading to an impact on annual operating profits in excess of \$250 million. This improved financial performance would typically be driven by 20 to 25 percent higher sales capacity per branch and 40 to 50 percent higher sales capacity per full-

time employee (due to greatly increased efficiency of lead generation and customer servicing), 40 to 50 percent lower customer attrition (due to greater loyalty driven by superior customer engagement), and 20 to 30 percent lower customer-acquisition and maintenance costs.

For smaller “attacker” banks (that is, banks with annual revenues under \$5 billion, fewer than 2,000 branches, and between 1 million and 5 million customers), the typical impact would be an increase of \$75 million to \$200 million in annual revenues and a \$50 million to \$150 million improvement in annual operating profits.

Capability building at scale: The necessary ingredient to sustain the impact of next-generation productivity-improvement initiatives

Capturing the benefits of a technology-enabled sales model at scale requires financial-services players to invest significantly in building the skills and capabilities of both the frontline and back-office staff. Capability building at scale is thus critical to ensure rapid and sustainable impact.

In reality, most players view capability building as a one-time investment focused on issuing new operating guidelines and training manuals and holding some classroom training. This approach often has limited effectiveness and is fundamentally incapable of achieving a radical shift in the way people work. To successfully embed the revised sales model at scale requires a very different approach, one focused both on skill building and on shifting the mind-sets and behaviors that usually act as barriers to the adoption of changes.

In our experience, a “field and forum” approach can be highly effective. This approach combines forums—classroom sessions to introduce and practice the new tools and operating procedures—with fieldwork, where specific projects are undertaken, allowing staff to practice new skills. This ensures the training is engaging and there is a high degree of retention.

Moreover, the field-and-forum approach addresses “softer” behavioral aspects by proactively surfacing underlying mind-sets (for instance, through individual and team reflection using standard tools) and then designing interventions to reinforce the right behavioral shifts (including role modeling of the change by senior staff, streamlining key performance indicators, and implementing incentives to support the changes required).



Technology-enabled sales will likely be the next big disruptive trend and could separate winners from losers in Asia's retail banking landscape. Banks must launch an integrated four-pronged initiative to tap into opportunities that technology offers to improve sales productivity and outpace competitors.

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Chapter 6

Four innovative ways to create actionable insights from customer data

Kenny Lam

Key highlights of this article:

- Banks are awash with customer data but many do not know how to leverage data into actionable insights.
- There are four proven ways of leveraging these data as seen from our experiences—they will help with differentiating frontline's approaches to relationship building, defining the next products to sell to customers, aligning the right channels for the right products and capabilities, amongst others.

Service is among the top attractions for consumers to Asian retail banks, ranking above products and convenience—but overall satisfaction is not high. By differentiating against competitors with targeted customer service, banks can stand to gain more market share, both through expanding their customer base and deepening relationships with existing customers. Yet with a finite amount of resources to deploy, banks need to find ways to align service and sales with customer needs and priorities.

The data advantage

Many customers value branch convenience as an aspect of service, for example, but only a limited number of banks will be in a position to capture that opportunity. Banks can, however, take advantage of many other opportunities to capture more value through better and more focused customer-portfolio management.

By customizing and right-sizing their service and product offerings, banks can intensify or expand their relationships with high-potential customers, while

effectively managing costs in lower-value segments. The key to unlocking this value lies in leveraging the vast amount of customer data that banks now have at their fingertips. Pertinent data sets will more closely establish customer value to the bank, by customer type and segment; banks can then address their customer relationships with greater focus and relevance in products, pricing, and channel.

Leveraging granular customer data can help banks

- capture a greater share of market segments and deeper penetration (wallet share) of existing customers (that is, for the affluent segment, in the areas of wealth management and investments)
- increase the effectiveness of cross-selling, enhancing the ratio of products per customer as well as “customer stickiness”
- increase and enhance the customer experience, based on a targeted approach to customer relationships, including greater focus on the direct sales force and aligned and enhanced high-function remote channels.

Practical insights on four levers

Banks can use their data to create actionable insights in four areas. These levers derive their effectiveness from upgraded analytics based on banks’ existing data:

1. Analyze customer composition to define and prioritize the relationship approach for different customers, based on customer value to the bank.
 2. Identify and size untapped cross-product opportunities among particular types of customers, using bank and benchmark data.
 3. Help the front line with an up-to-date “propensity to buy” model, which demonstrates the historical probability for next-product purchases by existing customer type.
 4. Identify underused channels by product, to expand opportunities for cross- and up-selling.
1. Prioritizing customer groups and defining the relationship approach for each

The application of this lever involves leveraging customer data to guide customer portfolio management. Resources can then be aligned accordingly, and a customer lens on overall performance can be developed and

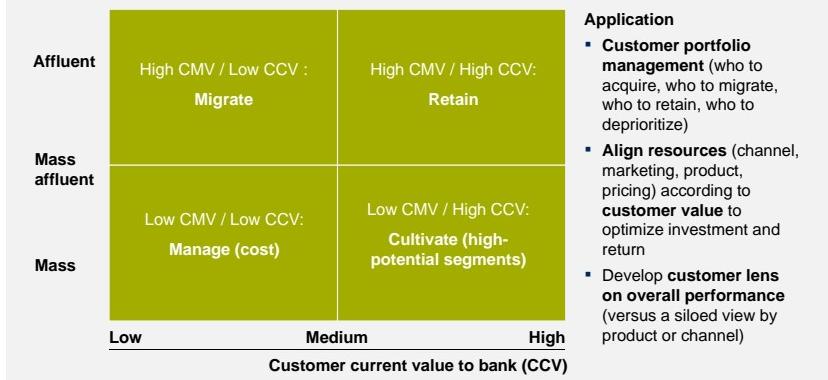
continuously refined. Many banks have well defined and relatively accurate models that use quantitative and qualitative information to estimate the total volume of customers. Customer-market value (CMV) is tracked through these models. A customer-value view—the customer's current value (CCV) to the bank—is obtained by laying CMV over the customer segments. The customers identified as having high CCV can then be given the focus they deserve, with the aim of creating deeper, enduring relationships throughout their financial life.

Exhibit 1 provides an example of how deeper analytics enabled by granular customer data allow banks to manage their customer portfolios beyond basic segmentation. Here four customer groups are defined and separately identified for retention, migration, expansion (acquisition), or deprioritization. Resources can then be aligned and allocated efficiently. Customers can be managed using the optimal channel, or channels, and marketing and product offers can be suitably customized to enhance customer value. The process also creates a customer lens on overall performance, a superior view than the typically siloed tracking of products or channels.

Exhibit 1

Leveraging vast data helps banks define and prioritize customer relationships.

Customer market value (CMV)

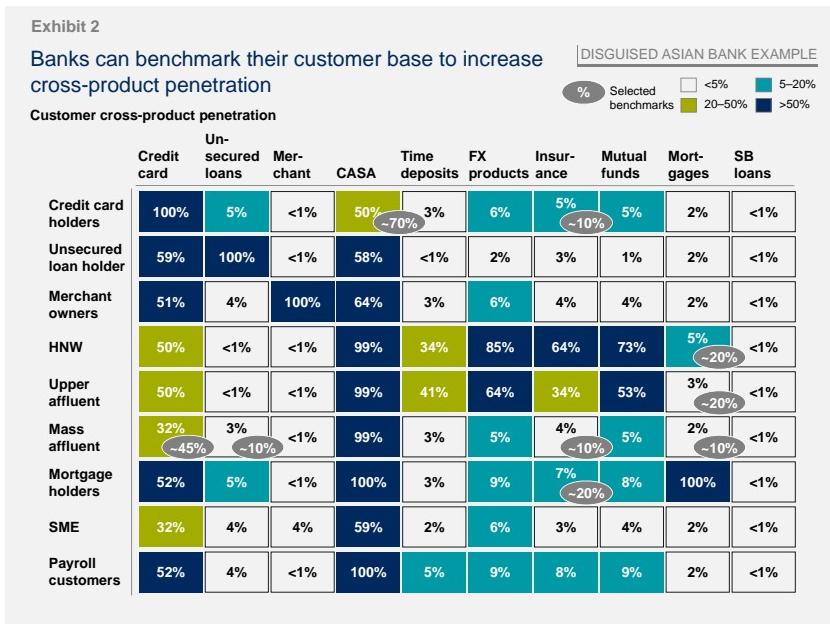


2. Finding opportunities to raise product penetration among existing customers

Banks can analyze and benchmark their customer base to reveal opportunities for achieving deeper cross-product penetration. All customer categories,

including wealth segments and customer types (mortgage holders, card holders, SMEs, etc.) can be benchmarked against best-practice financial institutions across the entire suite of the bank's offerings. When benchmarked cross-sell percentages are laid over the bank's actual cross-product-penetration levels, opportunities appear as shortfalls. These can then be sized and analyzed on a case-by-case basis to create targeted priorities within the bank's grasp.

Exhibit 2 offers a sketch of just such an analysis undertaken by a large Asian bank. The percentages in the ovals indicate the products and customer categories on which the bank is now focusing its cross-selling efforts based on its enhanced knowledge.



3. Arming the front line with a “propensity to buy” model based on the latest historical data

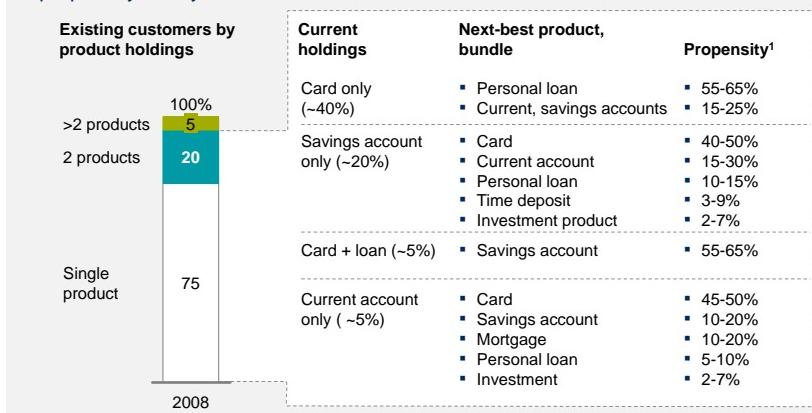
Banks' frontline resources are often expected to fashion cross-selling priorities and targets from static models and all-purpose key performance indicators. Yet banks can give the front line a much more effective “propensity to buy” model by simply leveraging their existing pools of customer data. Each customer category, defined by current holdings, can be matched to the next-best products or bundles, defined by historical likelihood for cross-sell (propensity to buy). The model, simple in itself, is periodically refreshed

based on the latest data on the bank's customer base. By giving the front line up-to-date knowledge of how different categories of customers tend to behave, resources can be concentrated on realistic targets and mutually rewarding relationships (Exhibit 3).

Exhibit 3

Banks can help the frontline with a dynamic
“propensity to buy” model.

DISGUISED ASIAN BANK EXAMPLE



¹ Based on historical propensity of top 25% product holders; propensity based on multivariate propensity models

4. Realizing the potential of sales channels to execute on product categories

Banks understand that certain products sell better through particular channels and they orient their sales and marketing accordingly. Everyone knows that mortgages are not sold online, nor are complex investment products sold through telemarketing calls. However, the number of sales channels through which certain products are sold can be expanded, using upgraded analytics based on the bank's own customer data. A product-by-product analysis of each of the bank's sales channels will reveal channel opportunities outside traditional patterns. These are channel-product pairings in which sales have occurred but not on a systematic basis. These opportunities can then be evaluated and judiciously operationalized according to the size of the opportunity and the bank's specific targets (Exhibit 4).

Sometimes the front line in the channels selected for expansion will not need product-specific retraining, but it should be kept in mind that fruitful

expansions can also occur in channels where some retraining is required. Either way, enhanced sales-channel potential is captured from the bank's existing resources by leveraging the bank's existing data, adding overall value with little added cost.

Exhibit 4

A product-specific analysis of sales channels reveals opportunities beyond the usual patterns

DISGUISED ASIAN BANK EXAMPLE

■ Existing primary product sales ■ Suitable but not used ■ Not fit
 ■ Existing secondary product sales ■ Suitable after retraining

Product categories	Sales channel											
	Branch		Tele-sales					Direct sales force				
	FA	Teller	Mutual fund	Service reps	Insurance	Loans	Cards	Loan FA	SME FA	Card (merchant)	Card (credit)	Payroll
Deposit account												
FX account												
Repurchase bond												
Mutual funds												
Advanced investment												
Traditional ins.				★	★					★	★	
Unit link ins.								★		★		★
Mortgage ins.										★		
Cash mgmt.										★		
Mortgage											★	
Personal loan												
SB loan										★		
Merchant												
Payroll												
Credit card												
Card loans, services												



As Asian banks struggle to maintain their margins even as they increase revenue, expectations are dropping and forecasts point to the situation remaining static. In such an environment banks seek to keep the customers they have, explore the potential for greater penetration, and reach out to attract new customers. To serve these purposes, banks already possess a powerful leverage-creating tool in the enormous amount of customer data they have compiled. This storehouse of potential knowledge can yield deep customer insights through proper analysis of the pertinent data sets. These insights in turn can be used to optimize customer relationships, align channels, and energize the front line with the richest and most relevant customer knowledge.

Smart, targeted use of the right data can open pockets of growth across the bank. As these are addressed and customer relationships realigned, the bank's resources can begin to show that greater returns are being achieved for the efforts expended. With the right orientation toward its customers, banks have the best chance of growing relationships to their full potential—over the multifaceted financial life of the customer.

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Chapter 7

Getting into the revenue flow: Insights from McKinsey's Asia-Pacific Payment Map

Vinayak HV, Florent Istace, and Raj Kamal

Key highlights of this article:

- Asia is likely to drive global payments revenue growth accounting for ~50% of incremental revenues (excluding accounts) over 2010-2015
- On an average, share of accounts in Asia payments revenues is comparable to Europe and Latin America, though there are significant inter-country variations
- Electronification of payments, across retail and corporate, is expected to increase to 83% of flows (up from the 64% in 2010), especially driven by emerging Asia
- Given the robust growth, competition is likely to intensify across non-bank payments players, local Asia-Pacific banks, and regional / global players

The vast Asia-Pacific region accounts for nearly three-quarters of global payment transactions. It is only recently, however, that payments revenues surpassed those of Europe and North America to take a global lead. In 2010, revenues of U.S. \$336 billion represented 31 percent of the global total, roughly in line with the region's 30 percent share of global GDP. Revenues are also growing faster in Asia-Pacific than in other regions, as consumers shift away from cash and toward electronic payments, and large and mid-sized corporations become more sophisticated and demand more services.

Opportunities in the region have naturally drawn the attention of payments players around the world. Specialists such as card processors, networks and even telcos are investing to capture a share of the pie. International banks are working on entry strategies. And local innovative specialists are seeking to solidify their current standing. For incumbents and disruptors alike, McKinsey's most recent Asia-Pacific Payments Map offers insights that can point the way to success in the region.

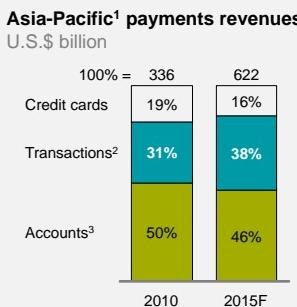
Transactions: More lucrative than expected

Accepted wisdom states that the lion's share of payments revenue in Asia-Pacific derives from accounts (current account and overdrafts net interest income, maintenance and incident fees) rather than from transactions. But at 50 percent, Asia-Pacific's reliance on accounts revenue is on par with Europe's (54 percent) and Latin America's (47 percent). (North America is the outlier at 28 percent, thanks to the prevalence of net interest margins earned on revolving credit card balances.)

Of course, the Asia-Pacific payments market is far from homogeneous, with stark differences between developed and developing countries in particular. In most developing countries (China, India, Thailand, Malaysia, Indonesia), account-related revenues still represent the vast majority of income, but transactions and credit cards are poised to increase rapidly, fueled by economic growth. Revenues in developed countries, meanwhile, are more evenly spread across accounts, transactions and credit cards, but account-related revenues will experience stronger growth driven by the inevitable recovery in reference interest rates from current historic lows (Exhibit 1). (South Korea is the exception; its sizeable credit card base provides the strongest foundation for growth.)

Exhibit 1

Share of accounts-related revenues is set to decline in Asia-Pacific.



1 Australia, China, Hong Kong, Korea, Japan, India, Indonesia, Malaysia, Singapore, Thailand, Taiwan

2 Debit cards, checks, direct debit, transfers, prepaid cards transaction fee income and float income

3 Current accounts and overdrafts, maintenance fee income and interest income

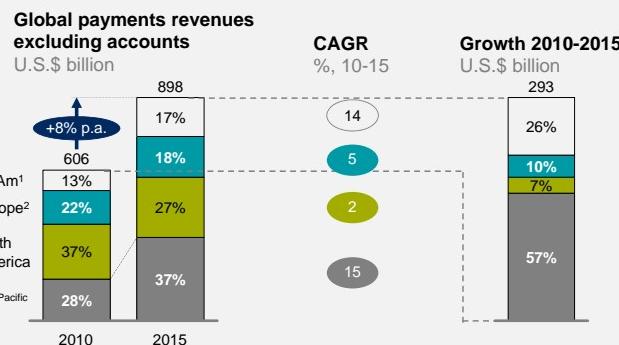
SOURCE: McKinsey Global Payments Map

Overall, however, the share of revenues from accounts continues to fall across the region, and is expected to drop to 46 percent by 2015, while credit card and transaction-related fee revenue income are on the rise. Asia-Pacific is projected to deliver 57 percent of global non-account payments revenue

growth over the next five years (Exhibit 2). This growth will present clear opportunities both for incumbents who already own banking relationships, and for attackers who can win the transaction business.

Exhibit 2

Asia-Pacific will account for 50% of global payments revenue growth, excluding accounts, over the next 5 years.



1 LatAm – Argentina, Brazil, Chile, Colombia, Mexico

2 Europe – EU27 excluding Luxembourg, Cyprus, Malta, Bulgaria and the 3 Baltics plus Norway, Russia and Switzerland

SOURCE: McKinsey Global Payments Map

New platforms, new opportunities

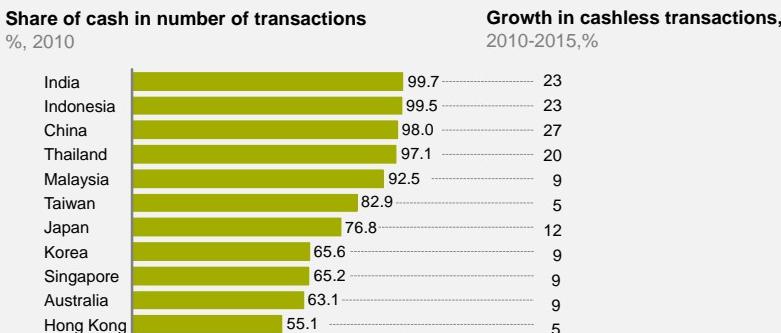
Across the region, although at different speeds, electronic payments (card payments, credit transfers and direct debits) are on the rise, at the expense of cash and checks. By 2015, electronic payments in Asia-Pacific should account for 83 percent of flows, up from 64 percent in 2010. This translates to an average annual growth rate of cashless transaction of more than 20 percent across Thailand, Indonesia, China and India, compared to 5 to 10 percent in South Korea, Japan and Australia (Exhibit 3) (See sidebar, “Where cash is emperor,” page 72). Given the higher revenues associated with electronic transactions compared to cash, this trend underscores the attractiveness of developing markets.

Driven by high levels of both adoption and innovation, flows for emerging payments methods such as prepaid cards and online and mobile payments will grow at more than twice the rate of overall payments flows over the next five years, especially in developing markets (Exhibit 4). Another clear sign of the prevalence of emerging payments in the region: 9 of the top 15 countries in MasterCard’s Mobile Payments Readiness Index are from Asia-Pacific. McKinsey’s Global Mobile Payments Survey confirms that excitement exists around the promise of

this technology: compared with developed markets like the U.S., U.K. and Hong Kong, a materially greater share of consumers in China and especially India expect mobile payments to be broadly accepted by retailers in three to five years. And in each country surveyed, well over half of consumers expect such broad acceptance within the same time frame. This strongly implies that mobile payments have the potential to disrupt payments habits across the region.

Exhibit 3

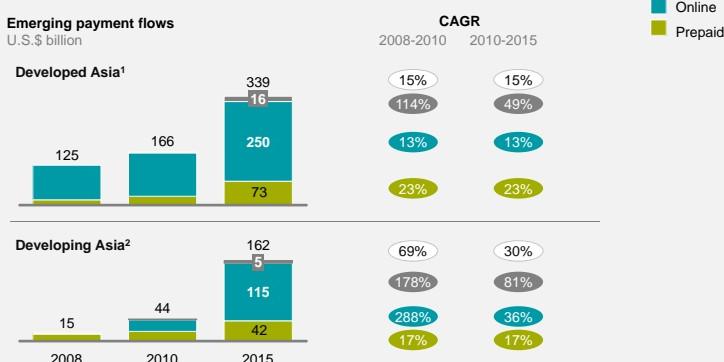
Asia-Pacific's cash intensive economies will see strong growth in cashless transactions.



SOURCE: McKinsey Global Payments Map

Exhibit 4

Emerging payments, particularly mobile, will experience extremely strong growth.



1 Australia, Japan, S.Korea, Taiwan, Hong Kong and Singapore

2 China, India, Indonesia, Malaysia and Thailand

SOURCE: McKinsey Global Payments Map; IDC New Media market model; Passport Internet retailing report; eMarketer Asia Pacific B2C ecommerce report

Prepaid card load is expected to grow at an average annual rate of 17 percent in Asia-Pacific through 2016, meaningfully higher than the already healthy 10 percent growth rate for the rest of the world. As always, specifics vary by market: prepaid cards have been enormously popular in China due to tax benefits which have led to payroll. Japan's prepaid business is highly transport-ticket driven, while in India fuel cards – seen as an expense management tool – are driving growth.

On the corporate payments side, the growing sophistication among corporate customers is providing further fuel for revenue growth. As an example, for the first time, providers' ability to integrate with enterprise resource planning systems ranks among mid-market customers' top three factors in bank selection, ahead of more traditional factors such as branch proximity. This implies that banks will need to invest to meet higher expectations on cash management solutions. By offering electronic marketplaces and ensuring that e-payments are secure and reliable (e.g., Alipay's escrow account solution), specialist players could capture share in this fast-growing market.

Large corporates meanwhile are consolidating their cash management relationships, especially for domestic services in China and India. There is also a strong demand for cross-border cash management solutions, given that many Asian corporates are rapidly expanding, particularly within Asia-Pacific itself (intra-Asia corridors account for more than half of total trade originating from the region). Here again, the revenue opportunity is substantial for those players with the capability and credibility to pursue it.

Competitive dynamics

Given the robust growth in the Asia-Pacific region, competition for revenues is likely to be intense. We see the competitive market being comprised of three categories of players:

- Non-bank payments players, including telcos, local payments specialists and global players, will innovate relentlessly to capture revenue. These players will need to differentiate themselves by providing innovative solutions to their existing customers, by bolstering their offerings both in terms of breadth and underlying technology. Already, players such as Alipay in China, Globe in the Philippines or PayPal across Asia-Pacific are establishing footholds. These firms will also need to improve the economics of their business (that is, grow to scale while improving pricing) and defend against the next wave of innovators.

- Asia-Pacific banks in home markets will need to protect their share of customer transactions and consequent revenue pools from both non-bank players and banks in non-home markets. This will have the effect of both reducing the revenue profile of accounts, and shifting transactions away from these banks. Already global banks such as Citi, HSBC and Standard Chartered have significant shares of the large corporate cash management business in many markets. In order to capture revenue in an increasingly electronified payments landscape, these banks will need to upgrade their capabilities and develop a culture of innovation, and exploit their strengths more effectively (e.g., supply-chain flows on the back of lending).
- Banks in non-home markets, both Asia-Pacific-based and global, will strive to win in specific niches while balancing regional/global business models with local customization. Given the large differences across Asia-Pacific, they will need to decide which markets and corridors they should prioritize. At the same time they will need to guard against the temptation to impose global business models and decision-making structures without understanding local customers, partners and regulators. It is also important to note that Asia-Pacific banks and non-bank players can upgrade their capabilities rapidly to become formidable competitors. The State Bank of India is a case in point; the recent upgrade of its cash management capabilities in a short time frame helped it capture a significant share of the mid-corporate space.

Where cash is emperor

Japan, with U.S.\$75 billion in revenues, is the fourth-largest country in the world in terms of payments revenues, behind the U.S., China and Brazil. Revenues come mostly retail current accounts (26 percent) and cards (37 percent).

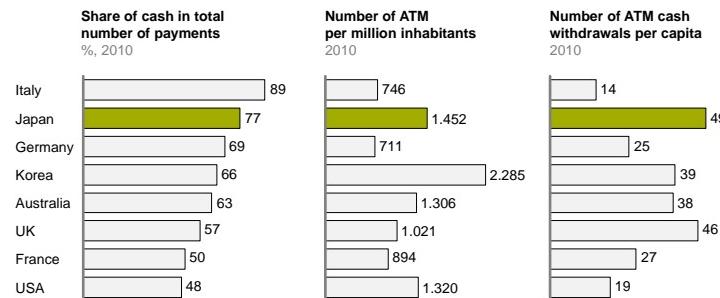
Although the population is often seen as tech savvy, Japan is actually more cash-based than many other developed economies. Just over three-quarters of transactions are cash, putting Japan between Italy and Germany, but a long way behind France or the U.S. High cash use translates into high ATM penetration and use, and indeed, the Japanese withdraw cash from ATMs about twice as often as French or American consumers (Exhibit A).

It's worth noting that although Japanese cards are mostly pay-later cards, card revenues come primarily from fee income (as in most European countries) rather than from net interest income (as in the U.S.). Japan and

France are the only countries where charge cards – also called deferred debit cards – are the most popular type of cards. Japan also generates more revenues from cash withdrawals and deposits than from credit transfers, direct debit and checks combined. Cash represents more than 10 percent of overall payments revenues in Japan, while in other developed countries cash typically accounts for 2 to 3 percent, once again confirming the love affair between Japan and cash.

Exhibit A

Japan has a love affair with cash and ATMs.



SOURCE: McKinsey Global Payments Map



There is little doubt that Asia-Pacific payments revenues will continue to grow at a healthy clip for the foreseeable future, comprising an increasing share of global revenues. Far less clear is the question of which players will win share of these revenues. The strategies pursued over the coming months will go a long way to define the Asia-Pacific payments landscape for the next several years.

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Chapter 8

The rise of Asia's private banking markets

Kenny Lam and Jared Shu

Key highlights of this article:

- Asia's private banking market offers substantial opportunity, but economics remain challenging (profit margins in the region are less than half of US and Europe)
- Onshore represents the largest potential and its dynamics are rapidly changing
- China will be the largest onshore market by 2015 and is still young and open to competition
- Given the diversity of the region, winning in Asia will mean adopting a much more targeted approach (onshore vs. offshore)

Asia's private banking market offers substantial opportunity, but economics remain challenging

Asia is poised to become the second-largest wealth management market in the world by 2015, just behind North America, attaining high net-worth (HNW) personal financial assets (PFA) of approximately US\$15.6 trillion. As such, it represents a significant opportunity for local, regional, and international private banks. Private banking is only beginning to take hold in the region, managing about 15 to 20 percent of all HNW assets, while prevailing levels of wealth-creation suggest strong growth potential. In addition, Asian private banking centers are benefiting from the reallocation of international clients' assets due to increasing interest in Asian markets and, to some extent, US flow to Asia-related funds, which has doubled over the past three years. Asian private banks enjoyed 7 to 9 percent net inflow over this same period. In fact, given the strong interest in the region, many customers today see Hong Kong and Singapore as natural alternatives to the more traditional offshore private banking centers (e.g., Switzerland). See Exhibit 1

Despite Asia's high growth rates, private banking economics in the region remain challenging, according to McKinsey's annual Private Banking Survey

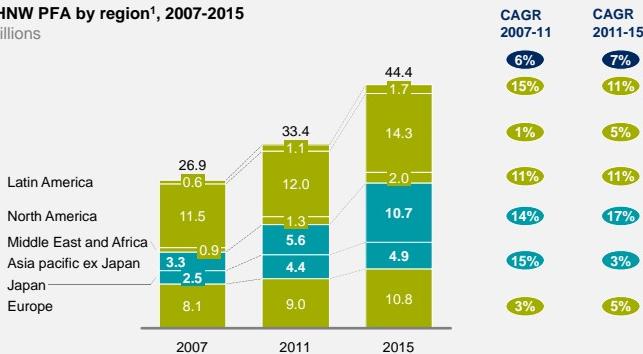
(first launched in 2002 and now covering all of Europe, the Middle East, Asia, and North America, with over 160 banks participating). In particular, average profit margins (as a percentage of assets under management) are relatively low vis-à-vis Europe and the US and have been on the decline, dropping from 20 bp in 2008 to 11 bp in 2011. See Exhibit 2.

Exhibit 1

By 2015, Asia will be the second largest wealth management market.

HNW segment is going to grow significantly in Emerging Markets

Total HNW PFA by region¹, 2007-2015
USD trillions



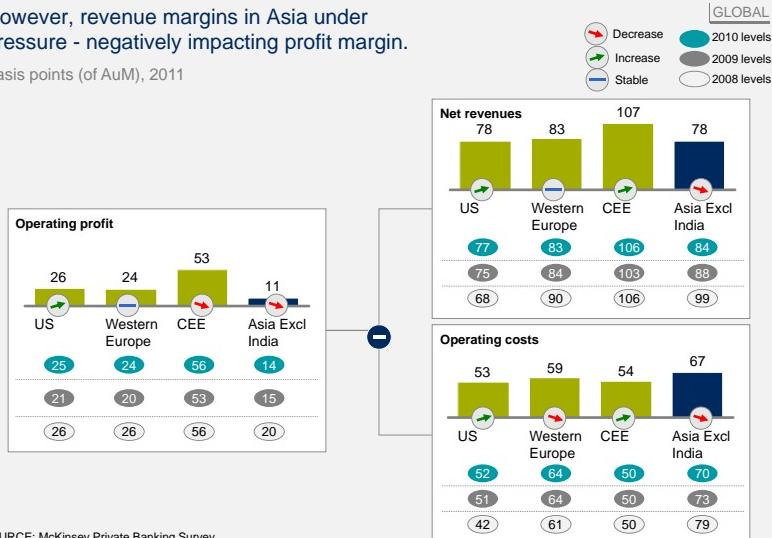
¹ Excludes Life Insurance and Pension onshore and offshore and does not include certain markets (rest of the world)

SOURCE: McKinsey Global Wealth Database

Exhibit 2

However, revenue margins in Asia under pressure - negatively impacting profit margin.

Basis points (of AuM), 2011



SOURCE: McKinsey Private Banking Survey

These declines are primarily the result of a drop in revenue margins, as private banking clients simplified their product portfolios and reduced their trading activity.

In addition, operating cost margins were relatively high in 2011, although lower than in previous years, at 67 bp. One explanation is that private banks' cost to serve has increased significantly due to rising RM compensation, paired with lower RM productivity and higher servicing requirements. Even as RM compensation has increased – the result of heightened demand for talent – RMs have become less productive due to less-entrenched client relationships, which make it harder for them to capture client assets. In fact, the average AuM per RM in Asia is about 20 percent below the European average. Adding to this, increased regulatory scrutiny post-crisis (e.g., more stringent customer-suitability checks) is leading to greater servicing requirements, boosting compliance costs. See Exhibit 3

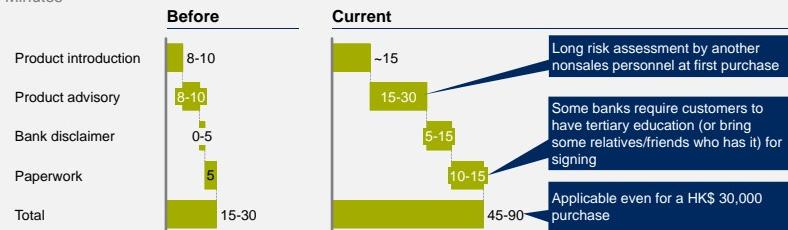
Note that performance varied enormously among the private banks in our survey, and the best-performing players have been able to achieve very healthy profit margins – in excess of 30 bp – because they have the scale to serve the HNW segment cost-effectively and have successfully differentiated their segment offerings.

Exhibit 3

Cost to serve is also likely to increase as banks are now taking 2-3 times longer to sell than before the regulatory changes.

Customer time to purchase mutual fund
Minutes

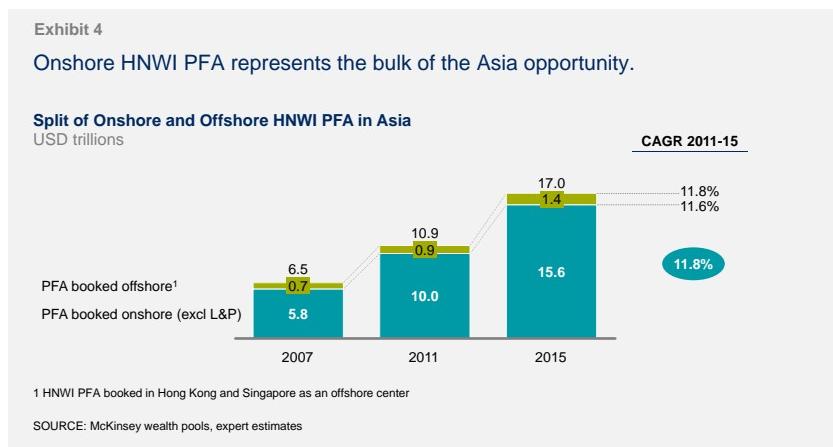
| EXAMPLE BANK IN ASIA



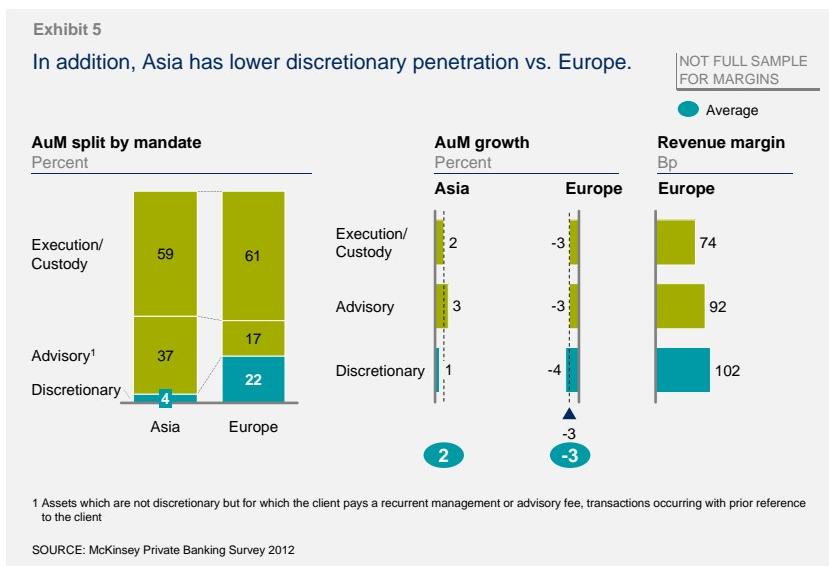
SOURCE: Literature search; interview; team analysis

Onshore represents the largest potential and its dynamics are rapidly changing

Despite relatively low returns, the potential of Asia's private banking market – especially in the onshore HNW segment – is strong. Onshore PFA currently represents over 90 percent of all PFA booked and managed in Asia (including the main offshore booking centers of Hong Kong and Singapore). See Exhibit 4



However, two important challenges persist in Asia's onshore markets. First, there are a number of regulatory product restrictions, both in mature markets such as Taiwan and in emerging markets such as China. In China, for example, retail investors cannot directly purchase offshore funds. Second, clients in Asia are still primarily self-directed; as a result, the share of discretionary mandates is much lower than in more developed markets such as Europe. See Exhibit 5



At the same time, we see four key trends that will shape Asia's private banking market over the next 5 years:

5. **Rise of entrepreneurial wealth** – The rapid economic growth in the region has been fueled largely by the growth of small and medium enterprises (SMEs); as a result, we estimate that over half of all HNWIs in Asia today are entrepreneurs. In addition, we estimate that SMEs contribute over half of GDP in some of the region's major economies including Japan, China, and Taiwan.

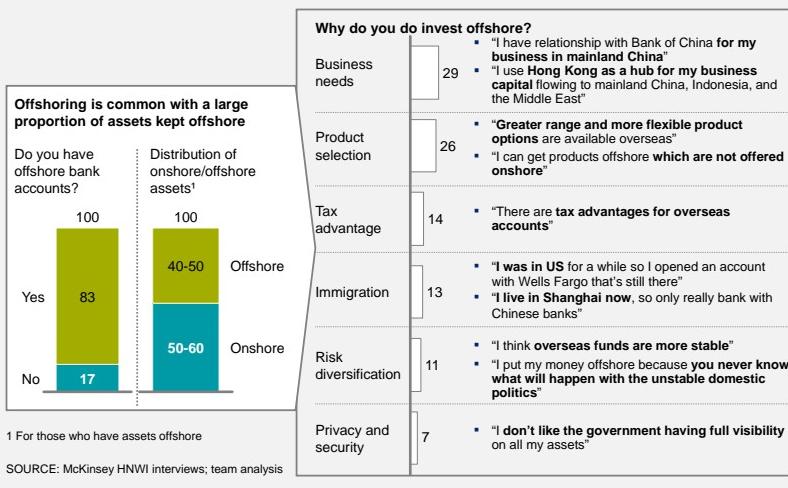
There is tremendous opportunity here, as a significant portion of entrepreneurial assets are still kept onshore, although offshoring continues to be common for these business owners due to their offshore business needs (e.g., setting up a trading company in Hong Kong). See Exhibit 6

Given the importance of the entrepreneurial segment, many private banks are still exploring different approaches to supporting it, e.g., providing services that cater to both personal and business needs. Going forward, more sophisticated levels of service, including succession planning and family offices (private companies that manage investments and trusts for individual wealthy families), will become increasingly important as the first generation of entrepreneurial wealth is transferred to the next.

Exhibit 6

Offshoring is common for business owners though a significant portion of assets are still kept onshore.

TAIWAN EXAMPLE

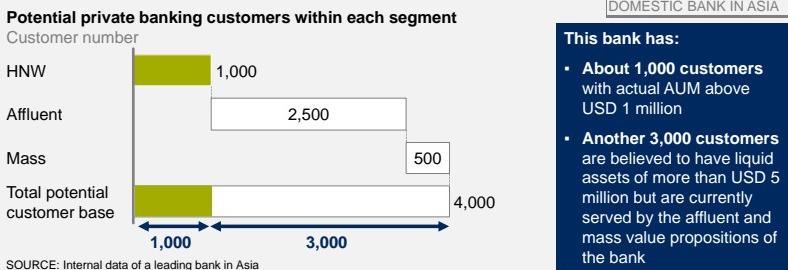


6. **Importance of the affluent** – With the rapid economic development in the region, we see wealth creation taking place across all key customer groups, in particular the HNW, affluent, and emerging-affluent segments. In many local commercial banks, the affluent segment – defined as individuals with PFA of US\$100,000 to US\$1,000,000 – represents over half of all PFA held in the bank. As a result, many leading local commercial banks are developing systematic approaches to identify and market to affluent customers with HNW potential. See Exhibit 7

Exhibit 7

Many banks sit on a large pool of potential HNW customers and migration of these customers will be a key source of AUM growth.

EXAMPLE: A LEADING DOMESTIC BANK IN ASIA



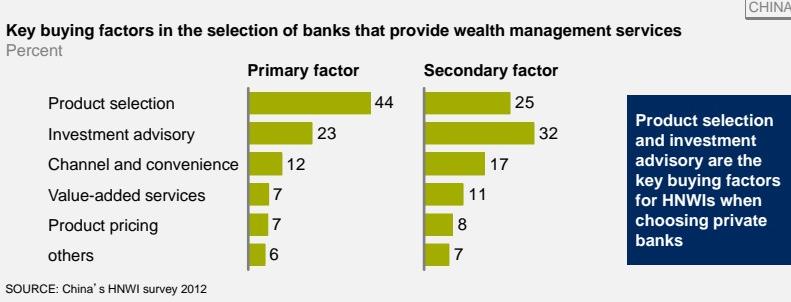
- 7. Role of investment advisory** – Customers from many of the emerging economies in the region are only beginning to understand the definition and services of a private bank. As a result, we expect the role of investment advisory to become increasingly important as penetration of private banking services continues to rise (currently roughly 15 to 20 percent of Asian HNW PFA).

However, there is some variation in the importance of investment advisory to customers across markets, depending on the maturity of the private banking sector in those markets. For example, in China, investment advisory ranks only second among a HNWI's key selection criteria when choosing a private banking provider, whereas in more mature markets such as Taiwan, investment advisory is the number 1 selection criteria. See Exhibit 8

- 8. Onshore to offshore** - A private bank moving into key Asian onshore markets (e.g., Taiwan or China) could see a positive knock-on effect as onshore customers spill over to their more profitable offshore business. The result could be a balancing out of profit margins in 8 to 10 years, depending on regulatory trends. The challenge for these banks will be to offset lower short-term returns with the high upfront investment needed to capture this longer-term potential.

Exhibit 8

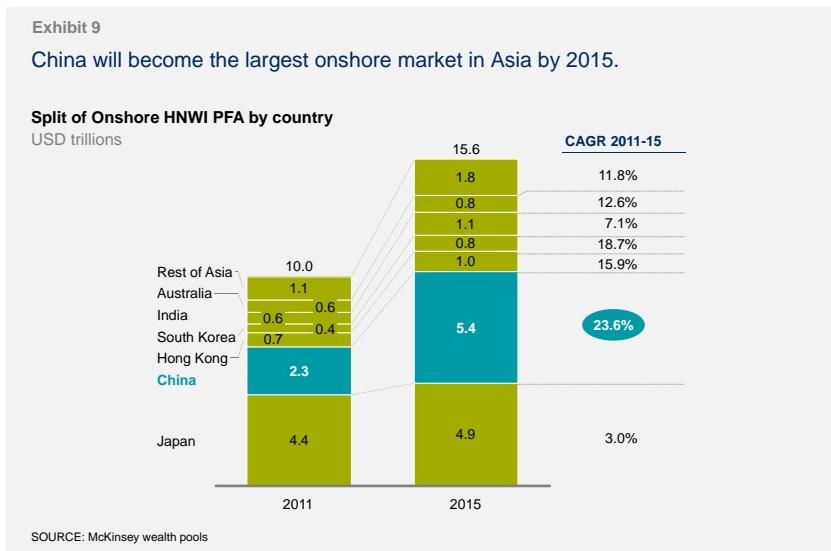
Product selection is the key buying factor.



China will be the largest onshore market by 2015 and is still young and open to competition

China is set to be Asia's largest onshore market by 2015, with onshore HNWI PFA expected to grow from US\$2.3 trillion to US\$5.4 trillion in the period from 2011 to 2015, for an astonishing CAGR of 23.6 percent. China's onshore PFA contribution as a percentage of Asian PFA will rise from roughly

23 percent in 2011 to 34 percent by 2015. In fact, China will contribute over half of the growth in Asia during the period from 2011-2015. See Exhibit 9



To take a closer look at this fast-growing market, McKinsey joined hands with China Minsheng Bank, China's largest non state-owned lender, to conduct a comprehensive deep-dive survey of 700 HNW individuals (defined as individuals with investible assets of greater than RMB 6.5 million or greater than USD 1 million) – the largest survey of its kind to date. Respondents, 100 of whom were interviewed face-to-face, were located in 29 Tier 1 and Tier 2 cities across China and provided tremendous insights into the wealth management needs, investment objectives, and demographics of China's high net-worth community.

Our survey uncovered a great deal of information about the demographics, preferences, and other characteristics of China's wealth management market and the HNWIs who constitute it. Some of the highlights include:

- The market itself is still open to competition, in part because so many HNWIs are unhappy with the private banking services currently on offer – or know little about the choices available
- Opportunities exist not only in China's largest, Tier 1 cities such as Shanghai and Beijing, but in Tier 2 cities as well, particularly those in China's growing coastal regions

- Product selection is a key consideration for China's HNWIs when choosing their wealth management provider, but it is not the only consideration; as in the rest of Asia, investment advisory is critical
- Onshore remains by far the most important HNW private banking opportunity
- Entrepreneurs represent the largest and most important segment by far, but serving them may be challenging due to wide variation in their investment requirements
- We have found that HNW business-ownersHNWIs can be grouped into six segments, each with its own distinct needs and preferences
- To win in this market, providers must be prepared to offer differentiated value propositions, while at the same time taking a close look at their own strengths and weaknesses – their location, customer base, branch network, offerings, partners and platforms – to understand how best to move forward

1. Still young

The market for private banking services in China is still relatively young. Although there has been tremendous growth in recent years, our survey found that China's private banking markets are still very much open to competition, with ample opportunities for new and non-Chinese players.

In fact, many HNWIs are unsatisfied with the private banking services they find on offer today. According to our survey findings, only 16 percent of private banking customers "highly agree" that they are fully satisfied with the level of private banking services they currently receive. Another 8 percent are clearly dissatisfied, while 30 percent are indifferent. Likely as a result, nearly half of all private banking customers allocate as little as 20 percent or less of their investable assets to their primary bank. Yet more than half say they would allocate 40 percent or more of these assets if the bank could fully satisfy their personal financial needs.

2. Beyond Tier 1

Going forward, we estimate the number of HNWIs and the number of ultra-high-net-worth individuals (UHNWIs) – those with investable assets of more than RMB 100 million or greater than USD 15 million – to grow by about 20 percent per annum from 2012 to 2015, reaching around 2 million and 130,000, respectively.

Perhaps surprisingly, a great many of these wealthy individuals live outside of the country's largest, "first-tier" cities of Shanghai, Beijing, Guangzhou and Shenzhen, instead inhabiting Tier 2 cities and below, particularly in the Yantze River Delta and Pearl River Delta regions. Tier 2 cities and below today make up nearly 80 percent of China's HNW wealth, compared to about 20 percent for the Tier 1 cities, and we expect their share of wealth to continue to grow.

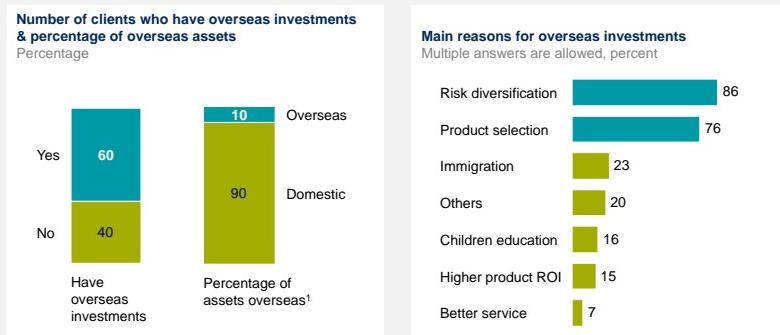
3. Onshore highlights

Our survey also found that onshore investments, as might be expected, remain by far the most important HNW private banking opportunities in China. While offshore investing is becoming more common – and many HNWIs express an interest, with 60 percent of those surveyed saying they currently have assets overseas – those who do invest offshore have only about 10 percent of their assets there. We note that the top two reasons given for offshore investing in China are diversification of risk and greater product selection. See Exhibit 10

Exhibit 10

It is common for Chinese HNWIs to have assets overseas and the reasons are mainly risk diversification and increased product selection.

CHINA



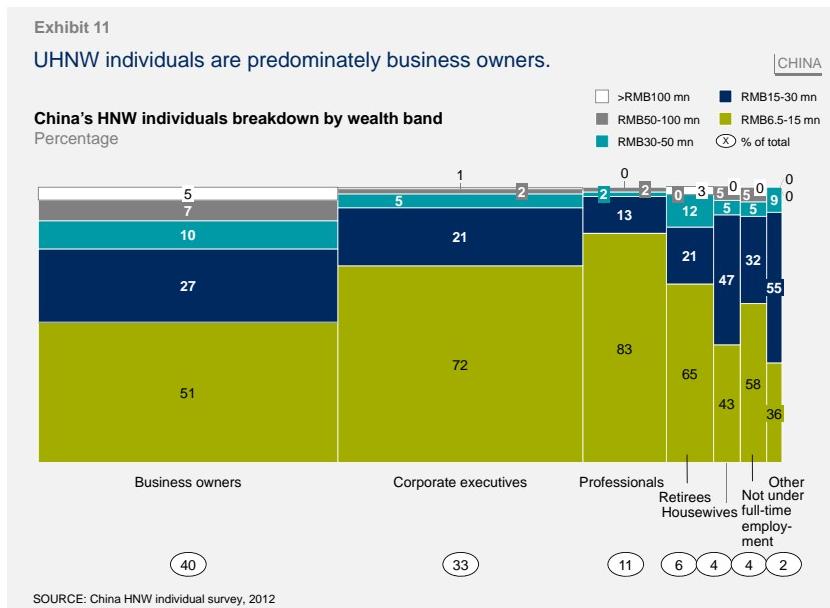
¹ For HNWIs who have overseas investments

SOURCE: China's HNWI survey 2012

4. Entrepreneurs lead

Just who are these HNWIs we care so much about? Our survey revealed a number of interesting demographic traits about the HNW segment, which is comprised primarily of males between the ages of 40 and 60. These wealthy individuals tend to be entrepreneurs or corporate executives who have at least a secondary-school education (higher than the national average). In

fact, entrepreneurs are the largest and wealthiest HNW group in China, representing as much as 40 percent of HNWIs. See Exhibit 11



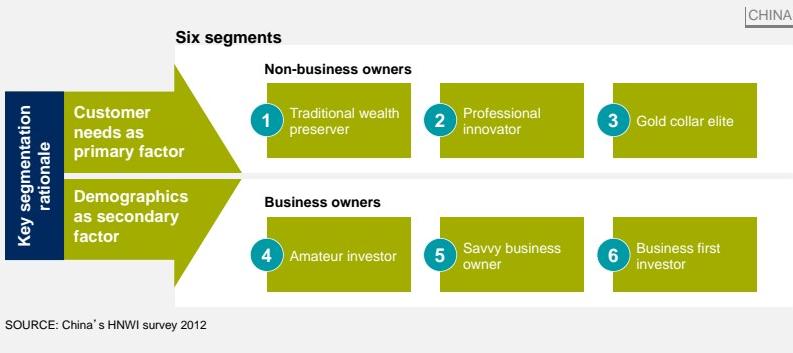
We note that focusing on this category of investors as a whole may be challenging for banks due to wide variations in investment requirements. In fact, business owners range from aggressive investors looking for active investment advice to those who primarily require convenience and access. The one thing they most have in common is their ambivalence towards using the same bank for both personal and business needs, with only 30 percent preferring to use the same relationship manager for both.

5. Six segments

For greater clarification, we used our knowledge of both demographics and customer needs to break down China's private-banking customers into six distinct segments, each with its own unique needs and preferences. These six segments can be grouped into two primary categories – business owners (e.g., entrepreneurs) and non-business owners. See Exhibit 12

Exhibit 12

China's HNWI can be categorized into 6 segments.



Among business owners, we identified three segments: the amateur investor, the savvy business-owner, and the business-first investor:

1. Amateur investors (20 percent of all HNWIs) prefer high-return products, but often lack investment knowledge and experience. They have a strong preference for a comprehensive array of products and seek banks that can tailor these products to their needs. To win in this segment, a private bank would require product breadth and superior investment-advisory services
2. Savvy business-owners (10 to 15 percent) rely less on their bank's service than other investors, as they often possess several years of investment experience and deep knowledge of banking products. These customers value privacy and therefore this segment is particularly unwilling to use a single bank for both personal and business needs. They are generally satisfied with their current private-banking provider, as they have done significant research prior to selecting it. To win in this segment, a private bank would require product depth and deep investment expertise, both at the RM and specialist levels
3. Business-first investors (10 percent) have a lower risk-tolerance than other investors. Their business and personal needs are closely linked and they value convenience. They are therefore more willing to use a single bank for both personal and business needs. To win in this segment, banks need to provide a distinctive multi-channel offering and a differentiated value proposition that combines both personal and business solutions

Among non-business owners, we identified three additional segments: the traditional wealth preserver, the professional innovator, and the gold-collar elite:

1. Traditional wealth preservers (25 to 30 percent of all HNWIs) have a lower risk tolerance than other investors and are often subject to the influences of market fluctuations and other individuals. They have more spare time than the average investor and a strong preference for a comprehensive array of products, and therefore value a bank's ability to tailor products to their needs. To win in this segment, banks would require a broad product offering and a high-touch RM coverage model
2. Professional innovators (15 to 20 percent) have several years of investment experience, deep knowledge, and high risk-tolerance, and tend to hold investment advisory services to a higher standard than most. They are generally satisfied with their current private-banking providers, as they have done significant research prior to selecting these banks. Private banks would require product depth and considerable investment expertise at both the RM and specialist levels to win in this segment. In addition, they would benefit from offering value-added services such as philanthropic advice
3. Gold-collar elites (10 to 15 percent) value convenience and easy access to remote banking channels. They possess some investment experience and knowledge but generally have less spare time than most investors. To win in this segment, banks would require a breadth of products and an effective multi-channel strategy

Given the diversity of the region, winning in Asia will mean adopting a much more targeted approach

Given the broad opportunities, challenges and complexities of the Asian private-banking market, providers must be prepared to focus. They cannot be everything to everyone in this diverse and fast-growing market; rather, they should offer carefully considered and differentiated value propositions to a select group of target segments and markets, focusing on both onshore or offshore accounts and determining how best to make the economics work for each.

For example, target customers may also be divided by wealth band (e.g., UHNW with over US\$30 million, HNW with US\$1 million to \$30 million); by origin of flows (e.g., Chinese, Southeast Asian, non-resident Indian, or Middle Eastern); by special requirements (e.g., small business owners, large family offices).

Meanwhile, choosing target markets will be different for every bank. The natural geographic markets for a new foreign-bank entrant, for example,

would be the offshore centers of Hong Kong and Singapore. However, banks may want to target select onshore markets to tap into the higher growth rates in domestic wealth.

For offshore success, we recommend the following

- Capitalizing on non-Asia client relationships (both retail and corporate) to capture offshore flows into Asia (mainly for global players)
- Adapting the current model to capture the region's largest offshore opportunity, e.g., addressing the offshore needs of entrepreneurs in the region
- Addressing core capabilities, including talent development and product and investment advisory platforms
- Exploring more innovative ways to serve the leading offshore markets, e.g., strategic partnerships

For onshore success, we recommend the following

- Developing anchor relationships with entrepreneurs onshore, e.g., providing a platform or service model that can address both an entrepreneur's personal and business needs. This anchor relationship onshore would hopefully translate into a relationship offshore.
- Building a core affluent-market value proposition to serve as a "feeder" for new customers to the private banking business. This advice is especially relevant for local players who already sitting on a large base of affluent customers who either have a lot of potential or are private banking customers in other banks.
- Investing in distinctive advisory platforms. This will be especially important as Asia's private banking market becomes more mature and the role of investment advisory increases in importance
- Exploring more innovative ways to serve the key onshore markets, e.g., mobile

Lastly, making private banking economics work will depend heavily on the choice of the end operating model. Shrinking profit margins in the region will require banks to be particularly adroit in designing an operating model that is effective and efficient, both in deepening their client relationships and in delivering profitability. Banks should think about whether to adopt a high-touch or a more hands-off model; what type of relationship managers are

needed and how to train them; and what type of platform (product platform, compliance, etc.) would work best. These decisions are especially important in Asia given that clients tend to be more transaction-focused, and classic high-touch private banking may not be the most appropriate model.

Each of these choices – target segments, markets, offshore vs. onshore, economics – will be dictated by a bank's own strengths and weaknesses: its location, customer base, branch network, offerings, partners, and platforms. The complexities and challenges of the Asian private banking market, and of China in particular, require a strategy and design for success – part of a considered approach to a powerful and ongoing market opportunity. May the best bank win.

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About us

McKinsey's Retail Banking Practice in Asia

McKinsey's Retail Banking Practice in Asia covers 13 markets with over 60 professional practitioners. We have served the leading retail banks across all of these 13 markets on a wide spectrum of issues—strategic or operational. Our Practice also has developed five special service lines and a series of proprietary data and research:

- Special service lines
 - Private banking and wealth management—building new propositions for new markets and helping existing operations substantially improve performance for the onshore and offshore markets
 - Customer centricity—developing implementable, impactful programs for customer centricity (from new approaches to customer service, to new channel developments)
 - Multi-channel management—redefining the role of branches and creating a seamless customer interface between channels (both traditional and new)
 - Sales transformation 2.0—using innovative (including new technology) means of quickly improving banks' productivity (with immediate bottom-line impact)
 - Digital banking—building new digital banking operations to attack new markets, or helping traditional banks develop new approaches to digital banking.
- Proprietary data / research
 - Asia Personal Financial Services Survey—the largest survey of banking customer behaviour in Asia with data from over 56,000 customer interviews since 1998
 - Private Banking Survey (Global and Asian editions)—operational data of over 350 private banks both globally and in Asia
 - China onshore private banking survey—in-depth research on private banking client needs in onshore China based on interviews with over 700 high net worth individuals

- Branch 360—proprietary data on branch-level competition (benchmarks against other banks) and customers (potential in the micromarket).

Authors

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